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Supreme Court, U.S.
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No.

IN THE

# Supreme Court of the United States

SONY MUSIC ENTERTAINMENT, ET AL.,

*Petitioners*,

v.

KEVIN STARR, ET AL.,

*Respondents*.

**On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit**

## PETITION FOR A WRIT OF CERTIORARI

THOMAS G. HUNGAR
*Counsel of Record*
JOSEPH KATTAN, PC
THOMAS M. JOHNSON, JR.
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 955-8500
thungar@gibsondunn.com

*Counsel for Petitioners*

## QUESTION PRESENTED

This Court recently reaffirmed that a complaint can survive a motion to dismiss only when the plaintiff "pleads factual content that allows the court to draw the reasonable inference that the defendant is *liable* for the misconduct alleged"—that is, when the facts alleged (if substantiated or proven) could satisfy the substantive legal standard that will govern the claim at summary judgment or trial. *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009) (emphasis added) (citing *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 556 (2007)). In the decision below, however, the Second Circuit rejected as "incorrect" the view that, in keeping with substantive antitrust law, plaintiffs "must allege facts that tend[] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior." Pet. App. 18a (alteration in original) (internal quotation marks omitted).

The question presented is whether the court of appeals erred in holding that a complaint can state a claim without alleging sufficient facts that, if proved, plausibly show an entitlement to relief under the substantive legal standard that will govern the claim at summary judgment or trial.

## PARTIES TO THE PROCEEDING

Petitioners in this Court, Defendants-Appellees below, are Sony Music Entertainment, f/k/a Sony BMG Music Entertainment; Sony Corporation of America; Universal Music Group; Warner Music Group Corp.; EMI Music North America; Capitol Records LLC, f/k/a Capitol Records, Inc., doing business as EMI Music North America; Capitol-EMI Music LLC, f/k/a Capitol-EMI Music, Inc.; and Virgin Records America, Inc. Time Warner Inc. and Bertelsmann, Inc., are not petitioners but were Defendants-Appellees below.*

Respondents in this Court, Plaintiffs-Appellants below, are Kevin Starr; Matt Putman; Cindy Seley, on behalf of herself and all others similarly situated; David Paschkett, on behalf of all others similarly situated; Christopher Michaud, on behalf of himself and all others similarly situated; Lisa Owens; Richard Benham, on behalf of himself and all others similarly situated; Keaton Landry, individually and on behalf of all others similarly situated; Sheri Clark; Rachel Hall; and Mitchell Horton.

## RULE 29.6 STATEMENT

Pursuant to this Court's Rule 29.6, undersigned counsel state that EMI NA Holdings, Inc.; EMI Group North America Holdings, Inc.; EMI Group In-

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* Although the case caption in the court of appeals also lists Bertelsmann Music Group, Inc., BMG Music, and BMG Music Publishing (doing business as The RCA Record Label) as Defendants-Appellees (*see* Pet. App. 1a), those entities were not parties to the proceedings below because they were not named as defendants in the Second Consolidated Amended Complaint. *See* Pet. App. 73a-76a.

ternational BV; EMI Group Holdings BV; EMI Group International Holdings Ltd; EMI Group Worldwide Ltd; Virgin Music Group Ltd; EMI Group Limited; Maltby Acquisitions Limited; Maltby Investments Limited; Maltby Holdings Limited; Maltby Capital Limited; and certain Terra Firma capital partner investment funds each have a direct or indirect ownership interest in petitioners EMI Music North America; Capitol Records, LLC; Capitol-EMI Music, LLC; and Virgin Records America, Inc. No publicly held corporation owns 10% or more of the EMI entities. Sony Corporation of America's parent company is Sony Americas Holding Inc., whose parent corporation is Sony Corporation, a publicly traded Japanese corporation. No other publicly held company owns 10% or more of Sony Corporation of America's stock. Sony Corporation, through various subsidiaries, holds 100% of Sony Music Entertainment. No other publicly held company owns 10% or more of Sony Music Entertainment's stock. Universal Music Group's indirect parent is Vivendi, S.A., a publicly traded company. No other publicly held corporation owns 10% or more of Universal Music Group's stock. Warner Music Group Corp., a publicly traded company, does not have a parent company. No publicly held corporation owns 10% or more of Warner Music Group Corp.'s stock.

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## PETITION FOR A WRIT OF CERTIORARI

Sony Music Entertainment, Sony Corporation of America, Universal Music Group, Warner Music Group Corp., EMI Music North America, Capitol Records LLC, Capitol-EMI Music LLC, and Virgin Records America, Inc. (collectively, the "Music Companies"), respectfully submit this petition for a writ of certiorari.

## OPINIONS BELOW

The court of appeals' opinion is reported at 592 F.3d 314. Pet. App. 1a-29a. The order denying rehearing or rehearing en banc is unreported. *Id.* at 30a-31a. The opinion of the United States District Court for the Southern District of New York is reported at 592 F. Supp. 2d 435. Pet. App. 32a-67a.

## JURISDICTION

The court of appeals filed its opinion on January 13, 2010. It denied the Music Companies' timely petition for rehearing or rehearing en banc on March 26, 2010. On June 15, 2010, Justice Ginsburg extended the time within which to file a petition for a writ of certiorari to and including August 23, 2010. No. 09A1214. The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

## FEDERAL RULE OF CIVIL PROCEDURE AND STATUTORY PROVISION INVOLVED

Federal Rule of Civil Procedure 8(a) provides in relevant part:

> A pleading that states a claim for relief must contain . . . a short and plain statement of the claim showing that the pleader is entitled to relief. . . .

Fed. R. Civ. P. 8(a).

The Sherman Act provides in relevant part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal.

15 U.S.C. § 1.

## STATEMENT

In a series of decisions, this Court has made clear that the sufficiency of a complaint under Federal Rule of Civil Procedure 8 is properly analyzed by testing the factual allegations of the complaint against the substantive legal standards that would apply to the claim at summary judgment or trial. Thus, in *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005), this Court held that when plaintiffs "need to *prove*" particular facts in support of a claim in order to prevail at trial, it follows that "the plaintiffs' complaint . . . [must] adequately . . . *allege* these [same] requirements." *Id.* at 346 (emphases in original).

Similarly, in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 553-54 (2007), the Court looked to substantive antitrust principles applicable at the summary-judgment, directed-verdict, and trial stages to hold that allegations of "conscious parallelism" or "parallel conduct" are insufficient to state a claim under Section 1 of the Sherman Act. The Court reasoned that such allegations fail to satisfy a plaintiff's obligation under Rule 8 to provide a "'showing'" of the "'grounds' of his 'entitle[ment] to relief'" that is sufficient to cross over "the line between possibility and plausibility." *Id.* at 555 & n.3 (citation omitted), 557. And in *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009), the

Court emphasized that the plausibility requirement applicable under Rule 8 is satisfied only "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is *liable for the misconduct alleged*," a determination that is necessarily governed by the substantive legal standards applicable at summary judgment and trial. *Id.* at 1949 (emphasis added).

The decision below conflicts squarely with these holdings. The Second Circuit explicitly rejected as "incorrect" the rule that plaintiffs asserting a Section 1 claim must allege sufficient facts in their complaint to satisfy the substantive legal standard that governs the claim at summary judgment or trial—namely, facts that "'tend[] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior.'" Pet. App. 18a (alteration in original); *see Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984).

In addition, having rejected the "tends to exclude" standard, the Second Circuit failed to test the plausibility of plaintiffs' allegations against lawful explanations for defendants' conduct. Rather, the court of appeals simply asserted that "plaintiffs have alleged behavior that would plausibly contravene each defendant's self-interest in the absence of similar behavior by rivals." Pet. App. 24a (internal quotation marks omitted). That conclusory statement contrasts sharply with the mode of analysis employed by this Court in *Twombly* and *Iqbal*, which involved a rigorous examination of "obvious alternative explanation[s]" for defendants' alleged behavior. *Twombly*, 550 U.S. at 567; *Iqbal*, 129 S. Ct. at 1951; *see also Dura*, 544 U.S. at 343.

The Second Circuit's decision also creates a conflict in the circuits over the proper interpretation of this Court's decisions in *Twombly* and *Iqbal*. Certio-

rari is warranted to resolve the conflicts between the decision below and decisions of this Court and other courts of appeals, and to provide additional guidance to the lower courts concerning the correct legal standards and criteria that govern review of the sufficiency of a complaint.

### A. Background and Plaintiffs' Complaint

Petitioner Music Companies are major producers and distributors of digital music files ("Digital Music"), which they sell either on compact discs ("CDs") or via the Internet ("Internet Music"). Pet. App. 3a. In 2001, two of the Music Companies, Universal Music Group and Sony, formed a joint venture called pressplay, and two others, Warner Music Group and EMI Music North America (along with Bertelsmann, Inc.), formed a joint venture called MusicNet. *See id.* These joint ventures were online services that sold Internet Music directly to consumers. *Id.* at 3a, 84a.

Since the late 1990s, peer-to-peer file-sharing services such as Napster (later enjoined for copyright violations, but which at that time had tens of millions of users) facilitated widespread unauthorized downloading of Internet Music free of charge. *See* Pet. App. 44a-45a. In this challenging economic environment, "the [Music Companies] that control the copyrights to most popular music [were] generally unwilling to license their music for online sale except in protected formats." *Id.* at 45a (second alteration in original) (internal quotation marks omitted). Thus, when the Music Companies launched their joint ventures, they entered into distribution agreements with either MusicNet or pressplay on terms and conditions (known as "Digital Rights Management" or "DRM" protections) designed to prevent unlicensed downloading and transferring of Internet Music. *See id.* at 3a, 44a-45a, 87a-88a.

Plaintiffs, alleged purchasers of Digital Music, sued the Music Companies under Section 1 of the Sherman Act for engaging in an alleged conspiracy to "restrain[] trade in and fix[] the price of Internet Music." *Id.* at 103a. According to plaintiffs, the Music Companies (acting through the joint ventures) distributed Internet Music pursuant to similar prices, terms, and conditions designed to "ma[ke] Internet Music less attractive to consumers, allowing Defendants to sell CDs at supracompetitive prices." *Id.* at 90a.

According to plaintiffs, the joint ventures and the Recording Industry Association of America ("RIAA") provided the Music Companies with "opportunities" and "forums" to communicate about prices and usage restrictions on Internet Music. Pet. App. 93a-94a. Specifically, plaintiffs allege that the Music Companies "agreed to a wholesale price floor . . . [for] Internet Music . . . at or about 70 cents per song." *Id.* at 96a. The Music Companies allegedly enforced this price floor by requiring retailers to sign Most Favored Nation ("MFN") agreements specifying that each of the Music Companies would receive terms from retailers that were as favorable as the terms received by any other Music Company. *Id.* In addition, both MusicNet and pressplay allegedly adopted "unpopular" DRM protections for downloadable Internet Music. *Id.* at 87a-88a. For example, plaintiffs allege that the joint ventures required users to pay regular subscription fees to access Internet Music and "did not allow transfer of the songs to portable digital music players such as the iPod." *Id.* at 88a.

Plaintiffs relied on isolated statements from industry participants and commentators, among other sources, to attempt to support their theory that this alleged parallel behavior amounted to an unlawful conspiracy. *See, e.g.*, Pet. App. 77a, 91a-93a, 95a-

96a. The complaint also quotes a commentator who stated that "nobody in their right mind" would want to pay $240 a year to subscribe to both MusicNet and pressplay. *Id.* at 89a. In the same article, however, that commentator also stated that one of the Music Companies' purposes in launching MusicNet and pressplay was "to protect their copyrighted works from freewheeling swapping on the Internet."[1]

### B. Proceedings In The District Court

The district court dismissed plaintiffs' complaint for failure to state a claim, relying on this Court's recent decisions in *Twombly* and *Iqbal*. Pet. App. 32a-67a. The court first set forth the substantive legal principles that govern review of Sherman Act Section 1 claims. Noting that the Act prohibits restraints of trade effected by "contract, combination, or conspiracy" (Pet. App. 41a (quoting 5 U.S.C. § 1)), the court held that "a § 1 violation based on 'tacit collusion' or 'conscious parallelism' requires more than a bare showing of parallel conduct." *Id.* (citing *Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 541 (1954)).

Accordingly, as the court explained, a plaintiff cannot prove a Sherman Act violation predicated on parallel business behavior without introducing evidence that "tends to exclude the possibility of independent action." Pet. App. 42a (quoting *Monsanto*, 465 U.S. at 768). Citing "the jurisprudence of 'plus factors'—the additional circumstantial evidence, beyond parallel conduct, that must exist to ensure 'that the inference of conspiracy is reasonable in light of the competing inferences of independent action'" (*id.*

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[1] Tom Spring, *Digital Music: Worth Buying Yet?*, PC World, Jan. 18, 2002, *available at* http://www.pcworld.com/article/80564/.

(quoting *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986))), the court held that *Twombly* required such "'plus factors' or 'factual enhancements'" to "appear in a § 1 plaintiff's complaint." *Id.*

Applying the above principles, the district court held that plaintiffs' allegations did not tend to exclude the possibility of lawful, independent action. The court began by rejecting plaintiffs' attempt to base their conspiracy claim on the "conclusory and implausible" assertion that the joint ventures were mere shams designed to serve as forums to conspire. Pet. App. 44a. To the contrary, "some level of information sharing" inevitably occurs within a joint venture, and the plaintiffs' complaint (as well as a predecessor complaint) revealed that each joint venture's activities were "consistent with rational business decisions" on the part of the Music Companies. *Id.* at 44a-46a. The court observed that in "the context in which [these] entities were created," "an environment of widespread unauthorized downloading of Internet Music," alleged "'unpopular' use restrictions and compromise in . . . pricing structure are each consistent with a collaborative effort to address widespread music piracy." *Id.* at 44a-45a.

The court further explained that, to the extent plaintiffs alleged parallel pricing or use terms adopted by the Music Companies *outside* the joint venture context, the complaint failed to rule out the possibility that "each Defendant was motivated *on its own* by the same *permissible* impulses that motivated the group as a collective." Pet. App. 48a (emphases added). Indeed, the mere fact that the Music Companies' prices and use restrictions were allegedly "unpopular" was meaningless in an environment where the Music Companies were competing for business with free, unauthorized downloads: "[U]nder the circumstances of widespread pirating,

the fact that customers disliked each Defendant's attempt to secure its copyrights shows nothing." *Id.* at 51a.

Because *Twombly* "require[d] that [plaintiffs] plead further facts tending to show conspiracy," and plaintiffs had not done so, the court held that the complaint must be dismissed. Pet. App. 52a.

### C. Proceedings In The Court of Appeals

The Second Circuit reversed. Pet. App. 1a-29a. The court acknowledged that allegations of "parallel business behavior" are insufficient to survive a motion to dismiss, because such behavior is "'just as much in line with a wide swath of rational and competitive business strategy unilaterally prompted by common perceptions of the market.'" *Id.* at 11a (quoting *Twombly*, 550 U.S. at 553-54). The court held that, in order to state a claim under Section 1, plaintiffs must place the parallel conduct "'in a context that raises a suggestion of a preceding agreement.'" *Id.* at 12a (quoting *Twombly*, 550 U.S. at 557).

The Second Circuit then concluded that plaintiffs' complaint survived the Music Companies' motion to dismiss. Pet. App. 14a. The court recognized that "the claim of agreement rests on the parallel conduct described in the complaint" (*id.* at 19a), such as the creation of two joint ventures, parallel price movements, and adoption of similar usage restrictions on Internet Music. *Id.* at 14a-15a. The court concluded, however, that the complaint also alleged facts placing the parallel conduct in a "context" suggesting conspiracy. *Id.* at 16a-17a. In the court's view, the requisite "context" was supplied by an industry commentator's assertion that MusicNet's and pressplay's prices and terms were unappealing, one Music Company executive's statement lamenting the

"devaluation of music," and an allegation that the Music Companies tried to "hide" MFN agreements to elude antitrust scrutiny. *Id.* at 16a-17a; *see supra* at 5-6. The court also relied on the fact that the Music Companies raised their prices even though the costs of providing Internet Music had allegedly declined and a much smaller distributor of Internet Music from less well known independent artists (eMusic) charged $0.25 per song. Pet. App. 17a.[2]

In deeming these allegations sufficient to state a Section 1 claim premised on parallel conduct, the Second Circuit dismissed as "incorrect" the Music Companies' argument that, in keeping with principles of antitrust law, plaintiffs "must allege facts that tend[] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior." Pet. App. 18a (internal quotation marks omitted). The court therefore rejected the relevance of the district court's "plus-factor" analysis at the motion-to-dismiss stage, as well as the general principle that plaintiffs must allege in their complaint facts that, if substantiated through discovery or proven at trial, would entitle plaintiffs to relief. *See id.*

Having refused to apply the "tends to exclude" standard at the pleading stage, the court of appeals rejected the Music Companies' argument that the facts alleged in the complaint "would be entirely consistent with independent, though parallel, action." Pet. App. 23a (internal quotation marks omitted).

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[2] The court further noted that the Music Companies controlled 80% of the market for Digital Music and that the Music Companies' prices had been the subject of investigations by the Department of Justice and New York State Attorney General (both of which were ultimately closed without any suggestion that any antitrust violations had occurred). Pet. App. 16a-17a.

Indeed, the Second Circuit did not address the plausibility of *any* lawful explanations for the Music Companies' behavior, including the district court's conclusion—noted earlier by the court of appeals—that the alleged parallel pricing and other conduct "was not against defendants' individual economic self-interest when viewed against the backdrop of widespread music piracy." *Id.* at 9a. Rather, the court rejected in cursory fashion the possibility that the Music Companies acted independently by noting that a single industry commentator, cited in the complaint, had stated that "nobody in their right mind" would want to purchase Internet Music at the prices charged by pressplay and MusicNet. *Id.* at 16a.

Judge Newman—who authored the Second Circuit's decision in *Iqbal* that was reversed by this Court—concurred in order to "explore" what he described as "a perplexing aspect" of *Twombly*. Pet. App. 24a. In particular, he found "perplexing" this Court's reliance on established principles of substantive antitrust law as a basis for holding that allegations of parallel business behavior "fall[] short of conclusively establish[ing] agreement or . . . constitut[ing] a Sherman Act offense." *Id.* at 25a (internal quotation marks omitted).

Judge Newman expressed the view that "one may wonder why a complaint alleging [parallel business] conduct does not survive a motion to dismiss." Pet. App. 25a-26a. Ultimately, he concluded that *Twombly* preserves "the availability of an inference of an unlawful section 1 agreement from parallel conduct." *Id.* at 28a. Accordingly, he agreed with and reemphasized the panel opinion's rejection of the principle that the substantive legal standards applicable at summary judgment or trial also apply at the motion-to-dismiss stage: "Even in those contexts in which an allegation of parallel conduct will not suffice to take an antitrust plaintiff's case to the jury, it

will sometimes suffice to overcome a motion to dismiss and permit some discovery." *Id.*

## REASONS FOR GRANTING THE PETITION

This Court should grant review to address the profoundly important and recurring question whether a complaint must be dismissed when its allegations, even if substantiated, would not satisfy the substantive legal standard applicable to the claim at summary judgment or trial. This Court's recent cases interpreting Rule 8—*Dura*, *Twombly*, and *Iqbal*—show in a variety of contexts that a court reviewing the sufficiency of a complaint must first identify the legal standards that a plaintiff would need to meet in order to be entitled to relief. The court must then examine the complaint in light of those substantive standards to determine whether it "allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged" (*Iqbal*, 129 S. Ct. at 1949) and "possess[es] enough heft to 'sho[w] that the pleader is entitled to relief'" (*Twombly*, 550 U.S. at 557 (internal quotation marks omitted)).

The Second Circuit's decision is in direct conflict with these precedents, because it explicitly rejects the principle that the same substantive standards applicable at summary judgment and trial also apply at the pleading stage. The decision below is also inconsistent with the approach that other courts of appeals have taken to *Twombly* and *Iqbal*. For example, the Sixth Circuit recently held that the "tend[s] to exclude" standard applicable to Sherman Act claims at summary judgment or trial can "illuminate[] the plausibility" of conspiracy allegations at the pleading stage, and dismissed a Section 1 complaint based on alleged parallel conduct better ex-

plained by "independent" business decisions. *Tam Travel, Inc. v. Delta Airlines, Inc.*, 583 F.3d 896, 907 & n.7, 908-09 (6th Cir. 2009).

This Court's review is necessary to resolve these conflicts and to prevent plaintiffs from imposing costly discovery obligations on defendants based on factual allegations that fall "shy of a plausible entitlement to relief." *Twombly*, 550 U.S. at 559.

## I. THE DECISION BELOW CONFLICTS WITH THIS COURT'S DECISIONS IN *TWOMBLY*, *IQBAL*, AND *DURA*

The decision below held that plaintiffs need not allege facts that "tend to exclude" the possibility of lawful, independent action as an explanation for a defendant's conduct. Pet. App. 18a. This holding directly conflicts with this Court's decisions in *Dura*, *Twombly*, and *Iqbal*, which require a plaintiff to allege those facts in a complaint that the plaintiff will later need to substantiate at summary judgment or prove at trial. Certiorari is warranted to resolve the conflict between the decision below and decisions of this Court.

### A. This Court's Precedents Test The Sufficiency Of A Complaint Against The Substantive Standards Applicable On Summary Judgment Or At Trial

Federal Rule of Civil Procedure 8(a) requires "a short and plain statement of the claim showing that the pleader is entitled to relief," so as to "give the defendant fair notice of what the . . . claim is and the grounds upon which it rests." *Twombly*, 550 U.S. at 555 (internal quotation marks omitted). Although "Rule 8 marks a notable and generous departure from the hyper-technical, code-pleading regime of a prior era," it "does not unlock the doors of discovery

for a plaintiff armed with nothing more than conclusions." *Iqbal*, 129 S. Ct. at 1950. Rather, to satisfy the requirement that a plaintiff "show[]" entitlement to relief, a plaintiff must plead specific facts—not merely the "formulaic recitation of the elements of a cause of action" (*Twombly*, 550 U.S. at 555) or "an unadorned, the-defendant-unlawfully-harmed-me accusation" (*Iqbal*, 129 S. Ct. at 1949).

Moreover, the facts in a complaint "must be enough to raise a right to relief above the speculative level." *Twombly*, 550 U.S. at 555. Not any facts will do; rather, "[t]o survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a *claim to relief* that is plausible on its face.'" *Iqbal*, 129 S. Ct. at 1949 (emphasis added). In turn, a claim is deemed "plausible" "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is *liable* for the misconduct alleged." *Id.* (emphasis added).

In *Twombly* and *Iqbal*, this Court described the mode of analysis that a court must follow to determine whether factual allegations are "plausible" enough to survive a motion to dismiss. In both cases, the Court began the "plausibility" inquiry by identifying the legal principles governing liability under the cause of action at issue. In *Twombly*, "the Court found it necessary first to discuss the antitrust principles implicated by the complaint." *Iqbal*, 129 S. Ct. at 1947. To identify those principles, the Court noted that it had previously "hedged against false inferences from identical [business] behavior at a number of points in the trial sequence." *Twombly*, 550 U.S. at 554. For example, a plaintiff at summary judgment "must tend to rule out the possibility that the defendants were acting independently" (*id.*, citing *Matsushita*, 475 U.S. 574); a plaintiff showing nothing beyond parallel conduct is not entitled to a

directed verdict (*id.*, citing *Theatre Enters.*, 346 U.S. at 540-41); and a plaintiff must "include evidence tending to exclude the possibility of independent action" at trial (*id.*, citing *Monsanto*, 465 U.S. 752). The Court also noted that Judge Lynch, who authored the district court opinion in *Twombly*, "understood that allegations of parallel business conduct, taken alone, do not state a claim under § 1; plaintiffs must allege additional facts that 'ten[d] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior.'" *Id.* at 552 (citation omitted).

Given these principles, the *Twombly* Court indicated that the same substantive legal standards that apply at later stages of a case also apply at the pleading stage. As the Court explained, Rule 8 "requires a 'showing,' rather than a blanket assertion, of *entitlement to relief*," and thus obligates plaintiffs to allege facts sufficient to "satisfy the requirement of providing not only 'fair notice' of the nature of the claim, but also 'grounds' on which the claim rests." *Twombly*, 550 U.S. at 555 n.3 (emphasis added). Because the plaintiffs' allegations of parallel conduct failed to exclude "lawful, unchoreographed free-market behavior," the complaint "did not plausibly suggest an unlawful agreement." *Iqbal*, 129 S. Ct. at 1950 (citing *Twombly*, 550 U.S. at 567, 570). Indeed, even the plaintiffs in *Twombly* conceded the "requirement of plausibility and the need for something more than merely parallel behavior." 550 U.S. at 560; *see also id.* at 586 (Stevens, J., dissenting) (noting that the majority applied "tends to exclude" legal standard to evaluate *Twombly* complaint).

Similarly, in *Iqbal*, an action against certain federal officials for allegedly unlawful detention policies, the Court "beg[an] by taking note of the elements a plaintiff must plead to state a claim of unconstitutional discrimination against officials entitled to as-

sert the defense of qualified immunity." *Iqbal*, 129 S. Ct. at 1947. Reviewing the relevant case law, the Court held that "[w]here the claim is invidious discrimination in contravention of the First and Fifth Amendments, our decisions make clear that the plaintiff must *plead and prove* that the defendant acted with discriminatory purpose." *Id.* at 1948 (emphasis added).

In fashioning the proper pleading standard, this Court relied on cases that had been decided on summary judgment or at trial. *See Iqbal*, 129 S. Ct. at 1948 (citing *Church of Lukumi Babalu Aye, Inc. v. Hialeah*, 508 U.S. 520, 540-541 (1993) (summary judgment on some claims; trial on others); *Washington v. Davis*, 426 U.S. 229, 240 (1976) (summary judgment)). These cases established the principle that a plaintiff attempting to *prove* unlawful discrimination must demonstrate that a particular policy or practice was adopted "because of," rather than "in spite of," a plaintiff's protected characteristic. *Lukumi Babalu Aye*, 508 U.S. at 540 (quoting *Personnel Admin'r of Mass. v. Feeney*, 442 U.S. 256, 279 (1979)). This Court found that it "*follows*" that "respondent must *plead* sufficient factual matter to show that petitioners adopted and implemented the detention policies at issue not for a neutral, investigative reason but for the purpose of discriminating on account of race, religion, or national origin." *Iqbal*, 129 S. Ct. at 1948-49 (emphases added). Thus, in *Iqbal*, as in *Twombly*, this Court required the plaintiff to allege facts in a complaint that (taken as true) would satisfy the same substantive legal standard that applies at summary judgment or trial.

Even before *Twombly*, this Court had previously "alluded to" the importance of the Rule 8 "entitlement requirement" in *Dura*, 544 U.S. 336. *Twombly*, 550 U.S. at 557. In *Dura*, this Court considered what allegations were necessary for a plaintiff to

adequately plead loss causation in a securities fraud case. The plaintiffs argued that they had adequately pleaded loss causation by alleging that the price of the security was inflated at the time of purchase. *See* 544 U.S. at 338.

In rejecting that assertion, this Court surveyed the substantive law governing liability for securities fraud and determined that an inflated purchase price, standing alone, was insufficient to "*prove* that the defendant's misrepresentation (or other fraudulent conduct) proximately caused the plaintiff's economic loss." *Dura*, 544 U.S. at 346 (emphasis added). The Court concluded that the same legal standard applies at the motion-to-dismiss stage: "Our holding about plaintiffs' need to *prove* proximate causation and economic loss leads us also to conclude that the plaintiffs' complaint here failed adequately to *allege* these requirements." *Id.* In *Dura*, as in *Twombly* and *Iqbal*, the Court recognized that the same substantive legal standards apply to the pleading stage as to later stages of litigation.[3]

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[3] In *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506 (2002), which predated *Twombly*, this Court held that a Title VII complaint survived a motion to dismiss even though the plaintiff did not plead a *prima facie* case of discrimination under the burden-shifting framework that applies at summary judgment in cases based on circumstantial evidence. But the plaintiff in that case alleged facts—the "events leading to his termination, [] relevant dates, and [] the ages and nationalities of at least some of the relevant persons involved with his termination"—that raised a reasonable expectation that discovery would yield *direct evidence* of discrimination, which supplied an independently sufficient alternative basis for potential liability. *Twombly*, 550 U.S. at 570 (quoting *Swierkiewicz*, 534 U.S. at 514). By contrast, the theories of conspiracy underlying the complaints here and in *Twombly* were based on inferences from parallel business behavior—not allegations of actual agreement. *See id.* at 564 ("the complaint leaves no doubt that plaintiffs rest their § 1

### B. The Second Circuit Squarely Held That The Substantive Legal Standard Applicable At Summary Judgment And Trial Does Not Apply At The Pleading Stage

In direct contrast to the principle established by *Twombly*, *Iqbal*, and *Dura*, the Second Circuit held that the substantive legal standard against which the complaint is tested on a motion to dismiss need not be the same as the standard applicable at summary judgment and trial. By rejecting as "incorrect" the Music Companies' argument that the "tends to exclude" standard applicable at later stages of the case should also govern the sufficiency of the complaint under Rule 8 (Pet. App. 18a), the Second Circuit departed from the holdings and rationales of this Court's precedents governing this issue.

If the Second Circuit were correct that substantive legal standards applicable at later stages of the litigation process are not controlling at the pleading stage, this Court in *Twombly* could not have reached the conclusion that parallel behavior, standing alone, is insufficient to state a claim under Section 1. Nor could this Court in *Iqbal* have reached the conclusion that allegations of unlawful discrimination must show government action taken "because of," rather than "in spite of," a protected characteristic. *Iqbal*, 129 S. Ct. at 1948 (internal quotation marks omitted). The Second Circuit's rejection of the "tends to

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[Footnote continued from previous page]

claim on descriptions of parallel conduct and not on any independent allegation of actual agreement among the" defendants); Pet. App. 19a ("the claim of agreement rests on the parallel conduct described in the complaint"). Therefore, the plausibility of plaintiffs' allegations must be tested against the substantive legal standard governing "entitlement to relief" on those claims—namely, the *Matsushita* "tends to exclude" standard.

exclude" standard conflicts with *Twombly* and *Iqbal*, which looked to relevant summary judgment or trial standards to determine what facts a plaintiff must allege to render a claim "plausible."

In rejecting application of the *Matsushita* standard to test the sufficiency of plaintiffs' complaint, the Second Circuit repeated the same error that it committed five years earlier in the decision that this Court overturned in *Twombly*. *See Twombly v. Bell Atl. Corp.*, 425 F.3d 99 (2d Cir. 2005). In that decision, the Second Circuit noted that, "under the ordinarily applicable standard" at summary judgment, a Section 1 plaintiff "'must present evidence that tends to exclude the possibility that the alleged conspirators acted independently,'" sometimes referred to as "plus factors." 425 F.3d at 113-14 (quoting *Matsushita*, 475 U.S. at 588). The Second Circuit held, however, that the *Matsushita* standard was inapplicable at the motion-to-dismiss stage. *Id.* at 114.

This Court, of course, reversed, holding that "[a] statement of parallel conduct, even conduct consciously undertaken," is insufficient "without [some] further circumstance pointing toward a meeting of the minds." 550 U.S. at 557.[4] This Court's message should have been clear: The failure to plead "further circumstance[s]" that tend to exclude the possibility of lawful explanations for parallel conduct is fatal to a complaint. As the decision below confirms, how-

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[4] Likewise, in the Second Circuit's decision in *Iqbal*, Judge Newman, writing for the court, interpreted *Twombly* to apply only "in those contexts where . . . amplification is needed to render the claim plausible." *Iqbal v. Hasty*, 490 F.3d 143, 158 (2d Cir. 2007). This Court again reversed, holding that the plausibility test applies equally to "all civil actions." *Iqbal*, 129 S. Ct. at 1953.

ever, the Second Circuit continues to adhere to its contrary view of the law.

### C. The Second Circuit's Erroneous Standard Conflicts With This Court's Mandate To Consider Obvious Alternative Explanations For The Alleged Conduct

The court of appeals' rejection of the "tends to exclude" standard led it to reject another aspect of the mode of analysis that this Court prescribed in *Twombly* and *Iqbal*—the need to identify and assess "obvious alternative explanation[s]" for the defendants' alleged conduct. *Twombly*, 550 U.S. at 567; *Iqbal*, 129 S. Ct. at 1951. The court of appeals' failure to test the plausibility of the allegations in the complaint against obvious benign explanations for the defendants' behavior—notably, the desire to protect copyrighted music and prevent unauthorized downloads—deepens the conflict with this Court's decisions.

Under *Twombly* and *Iqbal*, once a court identifies the proper legal standard to apply to the complaint, it must then determine whether the plaintiff's well-pleaded factual allegations state a "plausible" claim for relief. In so doing, a court cannot simply treat a complaint's allegations as if they exist in a vacuum. Rather, in order to determine whether the facts alleged support a "*reasonable* inference that the defendant is liable for the misconduct alleged," the court must consider the existence and plausibility (or lack thereof) of lawful "alternative explanation[s]" for the defendant's alleged conduct. *Iqbal*, 129 S. Ct. at 1949, 1951 (emphasis added). Thus, "[d]etermining whether a complaint states a plausible claim for relief will . . . be a context-specific task that requires the reviewing court to draw on its judicial experience and common sense." *Iqbal*, 129 S. Ct. at 1950. In

the antitrust context, a complaint's "sufficiency turns on the suggestions raised by [the alleged] conduct when viewed in light of common economic experience." *Twombly*, 550 U.S. at 565.

In *Twombly* and *Iqbal*, the Court explicitly tested the complaint's allegations against alternative, lawful explanations for the defendant's conduct. For example, in *Twombly*, the plaintiffs alleged that the regional telephone service monopolies previously owned by AT&T (the "Baby Bells") violated the Sherman Act in part by entering agreements not to compete with one another following passage of the Telecommunications Act of 1996, which for the first time authorized the Baby Bells to enter each other's respective geographic markets. *See Twombly*, 550 U.S. at 567. The Court rejected plaintiffs' theory of conspiracy, because "if history teaches anything," the "obvious alternative explanation" for the Baby Bells' behavior was that the companies were accustomed to a regulated environment characterized by noncompetition and geographically limited markets. *Id.* "Hence, a natural explanation for the noncompetition alleged is that the former Government-sanctioned monopolists were sitting tight, expecting their neighbors to do the same thing." *Id.* at 568. Thus, the parallel conduct in *Twombly*, while "consistent with an unlawful agreement, . . . did not plausibly suggest an illicit accord because it was not only compatible with, but indeed was more likely explained by, lawful, unchoreographed free-market behavior." *Iqbal*, 129 S. Ct. at 1950.

This Court undertook the very same analysis in *Iqbal*. In that case, the plaintiffs alleged that the Attorney General and Director of the FBI had "arrested and detained thousands of Arab Muslim men . . . as part of its investigation of the events of September 11," and had subjected plaintiffs to particularly restrictive conditions by designating them "of high in-

terest," based on their race, religion, or national origin. *Iqbal*, 129 S. Ct. at 1951 (alteration in original) (internal quotation marks omitted). Drawing on "judicial experience and common sense," the Court found that these factual allegations did not plausibly suggest unlawful discrimination because "a legitimate policy directing law enforcement to arrest and detain" suspected terrorists would be expected to "produce a disparate, incidental impact on Arab Muslims." *Id.* The Court concluded that "[a]s between that 'obvious alternative explanation' for the arrests, and the purposeful, invidious discrimination respondent asks us to infer, discrimination is not a plausible conclusion." *Id.* at 1950-51 (quoting *Twombly*, 550 U.S. at 567). *Iqbal* thus confirms that a court must evaluate the plausibility of the plaintiffs' favored inferences in the light of alternative, benign explanations for the alleged facts. *Accord Dura*, 544 U.S. at 342-43 (noting that there were alternative explanations for the alleged lost share value, such as "changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price").

The rigorous scrutiny that this Court applied to the allegations in *Twombly*, *Iqbal*, and *Dura*—testing them against lawful alternative explanations—stands in sharp contrast to the Second Circuit's approach in the decision below. To be sure, the Second Circuit noted the district court's holding that "the imposition of the [allegedly] unpopular DRMs and pricing structure was not against defendants' individual economic self-interest when viewed against the backdrop of widespread music piracy." Pet. App. 9a. But rather than inquire whether this obvious alternative explanation rendered plaintiffs' claims implausible, the court of appeals concluded

that plaintiffs' allegations "plausibly contravene" each defendant's self-interest based on the opinion of a single industry commentator, cited in the complaint, who stated that "nobody in their right mind" would want to subscribe to both MusicNet and pressplay. *Id.* at 24a.[5] This mode of analysis, in direct opposition to *Twombly* and *Iqbal*, would allow plaintiffs to survive a motion to dismiss simply by making bare allegations of anti-competitive conduct, regardless of how implausible those allegations are in light of lawful alternative explanations for defendants' behavior.

* * *

Certiorari is warranted to resolve the conflict between the decision below and decisions of this Court. The Second Circuit's test, which rejects application of summary-judgment case law at the pleading stage in favor of an amorphous consideration of "context" unmoored to the correct legal standard, injects confusion, vagueness, and uncertainty into what was intended to be a straightforward evaluation of the sufficiency of the complaint's allegations. By contrast, this Court's decisions in *Dura*, *Twombly*, and *Iqbal* provide a ready (and obvious) source for identifying the facts that ought to appear in a well-pleaded complaint: the jurisprudence supplying the legal stan-

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[5] That commentator nevertheless acknowledged that the Music Companies' purposes in launching MusicNet and pressplay were "to protect their copyrighted works from freewheeling swapping on the Internet, and to pick up a few extra bucks for making the music available digitally." Spring, *supra* note 1. Under *Twombly*, a reviewing court is entitled to "take notice of the full contents of the published articles referenced in the complaint." 550 U.S. at 568 n.13 (citing Fed. R. Evid. 201). This article (as well as the extensive analysis provided by the district court) confirms that concern about piracy was an "obvious alternative explanation" for defendants' conduct.

dards that a plaintiff will ultimately need to meet to demonstrate "entitlement to relief" (Fed. R. Civ. P. 8(a)(2)). Contrary to the rule of law announced by the decision below, that jurisprudence in the antitrust context requires plaintiffs to plead facts that "tend to exclude" lawful, independent explanations for defendants' conduct.

## II. THIS COURT SHOULD GRANT REVIEW TO RESOLVE THE DISAGREEMENTS AMONG THE LOWER COURTS CONCERNING THE PLAUSIBILITY STANDARD SET FORTH IN *TWOMBLY* AND *IQBAL*

This Court's review is also warranted to resolve disagreements among the federal courts of appeals concerning the proper legal standard to apply in reviewing the sufficiency of factual allegations in a complaint. For example, in *Tam Travel*, the Sixth Circuit explicitly held that *Matsushita*'s "tending to exclude" standard can "illuminate[] the plausibility" of antitrust conspiracy allegations at the pleading stage. 583 F.3d at 907 n.7. The Sixth Circuit also correctly construed *Twombly* as holding that courts must "assess the plausibility of an alleged illegal agreement" at the pleading stage by examining whether the complaint alleges facts that tend to exclude "reasonable, alternative explanation[s]" for the defendants' parallel conduct. *Id.* at 908-09. Applying those rules of law, the Sixth Circuit affirmed the dismissal of a Sherman Act Section 1 claim because the "defendants' conduct 'was not only compatible with, but indeed was more likely explained by,'" lawful, unilateral decisions. *Id.* at 908 (quoting *Iqbal*, 129 S. Ct. at 1950).

Like the plaintiffs in this case, the travel agency plaintiffs in *Tam Travel* had asserted a Section 1 claim founded primarily on allegations of parallel

behavior. *See* 583 F.3d at 905. The plaintiffs alleged that the defendants, several major airlines, conspired to cut airfare sales commissions paid to travel agents. *See id.* at 898. The plaintiffs supported the conspiracy inference with factual allegations purporting to show that the airlines acted against their individual self-interests, including statements from airline executives supposedly showing coordinated price movements and specific allegations of private meetings between several airline executives. *See id.* at 908, 910-11.

Rather than simply accepting these allegations at face value, however, the Sixth Circuit recognized that *Twombly* "provides an additional safeguard against the risk of 'false inferences from identical behavior' at . . . the pleading stage" because it requires dismissal of Section 1 claims founded on conduct "*more likely explained by lawful, unchoreographed, free-market behavior.*" 583 F.3d at 904 (quoting *Iqbal*, 129 S. Ct. at 1950). Applying that standard, the court concluded that the facts alleged did not tend to exclude the alternative, plausible explanation "that each defendant had a reasonable, independent economic interest in adopting a competitor's commission cut." *Id.* at 908-09. As in *Twombly*, there was "'no reason to infer that [these defendants] had agreed among themselves to do what was only natural anyway.'" *Id.* at 909 (alteration in original) (quoting *Twombly*, 550 U.S. at 566).

By contrast, the Second Circuit in this case rejected as "incorrect" the proposition that a plaintiff "must allege facts that 'tend[] to exclude independent self-interested conduct'" to defeat a motion to dismiss, and therefore the court failed to test whether plaintiffs' allegations were more or less plausible than lawful, self-interested explanations for defendants' alleged behavior. Pet. App. 18a, 23-24a (citation omitted). For example, the court uncritically ac-

cepted the allegation that "some form of agreement among defendants would have been needed to render the [joint ventures] profitable," based on one commentator's remark that their usage terms were unpopular, *id.* at 16a—without considering whether the usage restrictions were more plausibly explained by the Music Companies' individual interests in preventing music piracy. The court thus ignored the crucial "safeguard" against false inferences of conspiracy that the Sixth Circuit carefully applied. The modes of analysis in *Tam Travel* and the decision below cannot be reconciled.

Widening the conflict among the courts of appeals, the Third Circuit recently adopted an approach to *Twombly* that attempts to chart a middle course between *Tam Travel* and the decision below. *See In re: Ins. Brokerage Antitrust Litig.*, No. 07-4046 (3d Cir. Aug. 16, 2010). In *Insurance Brokerage*, the Third Circuit recognized that "*Twombly* aligns the pleading standard with the summary judgment standard in at least one important way," in that it requires plaintiffs to allege more than mere parallel conduct to survive a motion to dismiss. *Id.*, slip op. at 51.[6] Accordingly, the Third Circuit concluded that "plaintiffs relying on parallel conduct must allege facts that, if true, would establish at least one 'plus factor,' since plus factors are, by definition, facts that 'tend[] to ensure that courts punish concerted action—an actual agreement—instead of the unilateral, independent conduct of competitors.'" *Id.* at 53

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[6] The court also stated (without fully elaborating) that while "*Twombly*'s articulation of the pleading standard for § 1 cases draws from summary judgment jurisprudence, the standards applicable to Rule 12(b)(6) and Rule 56 motions remain distinct." *Id.* at 52 n.21. In making this cryptic observation, the court noted, but did not adopt, the view expressed by Judge Newman in his concurrence below. *See id.*

(internal citation omitted). As this recent decision confirms, absent further guidance from this Court, the courts of appeals undoubtedly will continue to disagree about the proper relationship between pleading standards and summary judgment standards when reviewing a motion to dismiss.

The Second Circuit's decision in this case reveals a further, related way in which the courts of appeals are now divided. Unlike the Second Circuit below, other courts of appeals have consistently held that the *Twombly-Iqbal* plausibility inquiry requires a careful weighing of the plaintiffs' allegations against alternative, benign explanations for the defendants' actions. In *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585 (8th Cir. 2009), for example, the Eighth Circuit held that while "Rule 8 does not require a plaintiff to plead facts tending to rebut *all* possible lawful explanations for a defendant's conduct," *id.* at 596 (emphasis added), "where there is a concrete, obvious alternative explanation for the defendant's conduct," "a plaintiff may be required to plead additional facts tending to rule out the alternative." *Id.* at 597 (internal quotation marks omitted). This requirement, the court reasoned, was "a corollary of the basic plausibility requirement." *Id.* "An inference pressed by the plaintiff is not plausible if the facts he points to are precisely the result one would expect from lawful conduct in which the defendant is known to have engaged." *Id.*

Similarly, in *Insurance Brokerage*, the Third Circuit held that "*Twombly* makes clear that a claim of conspiracy predicated on parallel conduct should be dismissed if 'common economic experience,' or the facts alleged in the complaint itself, show that independent self-interest is an 'obvious alternative explanation' for defendants' common behavior." *In re: Ins. Brokerage Antitrust Litig.*, No. 07-4046, slip op. at 60-61. "Put differently, allegations of conspiracy

are deficient if there are 'obvious alternative explanation[s]' for the facts alleged." *Id.* at 52.

The reasoning in *Braden* and *Insurance Brokerage* cannot be squared with the decision below. Whereas the Eighth Circuit acknowledged that (under *Twombly*) there will be circumstances in which plaintiffs may be required to plead facts "tending to rule out" lawful explanations for defendants' conduct, the decision below held categorically that plaintiffs are *not* required to plead facts "tending to exclude" lawful, self-interested behavior. And *Insurance Brokerage* (unlike the decision below) makes plain that a reviewing court must scrutinize the allegations in a complaint to determine whether they accord with "common economic experience" or "obvious alternative explanation[s]" for the alleged illegal activity.

*Tam Travel* and *Braden* correctly reflect the principles enunciated by this Court in *Twombly* and *Iqbal*. *Tam Travel* recognizes the relevance to the Rule 8 inquiry of the substantive legal standards that govern a claim at summary judgment or trial, and both cases acknowledge that the plausibility of a plaintiff's conclusions cannot be isolated from the plausibility of obvious, alternative explanations for a defendant's alleged conduct. In both of these respects, *Tam Travel* and *Braden* are inconsistent with the decision below. And the Third Circuit's recent decision in *Insurance Brokerage* introduces additional confusion and uncertainty into this area of the law by adopting a test that attempts to split the difference between *Tam Travel* and the decision below. The Court should grant review to resolve these disagreements among the courts of appeals.

## III. THIS CASE RAISES IMPORTANT AND RECURRING ISSUES THAT REQUIRE RESOLUTION BY THIS COURT

Finally, this Court should grant review because this case presents recurring issues of great importance concerning the law of pleading in general and the context of antitrust litigation in particular. This Court has recognized the great "practical significance" of the Rule 8 requirement that a plaintiff must show an "entitlement" to relief to survive a motion to dismiss. *Twombly*, 550 U.S. at 557. "[W]hen the allegations in a complaint, however true, could not raise a claim of entitlement to relief, this basic deficiency should . . . be exposed at the point of minimum expenditure of time and money by the parties and the court." *Id.* at 558 (alteration in original) (internal quotation marks omitted). Permitting legally deficient claims to progress to the next stage based on "mistaken inferences" of wrongdoing imposes substantial costs. *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 414 (2004). The costs of such "false positive" errors include the toll on judicial resources and "potentially enormous" discovery costs. *Twombly*, 550 U.S. at 559.

The heavy burden of unwarranted discovery was an important consideration for this Court in *Twombly* and *Iqbal*. In particular, this Court noted in *Twombly* that "antitrust discovery can be expensive," and "'a district court must retain the power to insist upon some specificity in pleading before allowing a potentially massive factual controversy to proceed.'" *Twombly*, 550 U.S. at 558 (quoting *Associated Gen. Contractors of Cal., Inc. v. Carpenters*, 459 U.S. 519, 528 n.17 (1983)). "It is no answer to say that a claim just shy of a plausible entitlement to relief can, if groundless, be weeded out early in the discovery

process through careful case management," because judges historically have been lax in curbing discovery abuse and because "the threat of discovery expense will push cost-conscious defendants to settle even anemic cases before reaching those proceedings." *Id.* at 559 (internal quotation marks omitted).

Because the cost of "false positive[s]" is uniquely high in the antitrust context, it is crucial that district courts filter out claims based on allegations that do not rise to the level of collusion or conspiracy. *Twombly*, 550 U.S. at 554. By rejecting the applicability of "tends-to-exclude" analysis at the pleading stage, the court of appeals failed to provide district courts with the necessary tools to screen out meritless claims, thus injecting a new uncertainty into the review of antitrust complaints. In lieu of the "tends-to-exclude" standard, the court of appeals adopted and applied an open-ended "context" test that is unmoored from substantive antitrust principles. The virtue of the standard set forth in *Twombly* is that it draws on an established jurisprudence of "plus-factor" analysis. The Second Circuit's ill-defined "context" approach, by contrast, consists of judicial improvisation with a hodge-podge of alleged facts of indeterminate weight. Pet. App. 16a-18a. A test so amorphous cannot be relied upon to distinguish between unlawful collusion and parallel conduct that naturally results from firms reacting independently to the same market forces. *Twombly*, 550 U.S. at 553-54.

As a result, the court of appeals' rejection of the tends-to-exclude standard will subject defendants to costly, protracted Sherman Act litigation based on nothing more than lawful conduct that is common in dynamic markets. As economists and antitrust scholars have long understood, parallel pricing and conduct among market rivals is frequently the natural result of *procompetitive* behavior. *See* Richard A.

Epstein, AEI-Brookings Joint Center for Regulatory Studies, *Motions to Dismiss Antitrust Cases: Separating Fact from Fantasy* 3-4 (2006); Paul A. Samuelson & William D. Nordhaus, *Economics* 51-53 (18th ed. 2005) (noting that, in a competitive market, firms responding to the same forces of supply and demand will engage in similar and even parallel conduct). In view of these economic realities, conscious parallelism alone is "meaningless." Donald F. Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 Harv. L. Rev. 655, 681 (1962); *see also Theatre Enters.*, 346 U.S. at 541 ("'conscious parallelism' has not yet read conspiracy out of the Sherman Act entirely"). Indeed, as former Federal Trade Commission Chairman William Kovacic has observed, the *Matsushita* tends-to-exclude standard was devised to guard against "mistaken inferences from ambiguous evidence [that] might deter procompetitive or benign conduct." William E. Kovacic, *The Identification and Proof of Horizontal Agreements Under the Antitrust Laws,* 38 Antitrust Bull. 5, 28 (1993).

Critically, parallel behavior is not limited to pricing and may also include imitation of a rival market participant's innovations or other business strategies. *See* Marvin Lieberman & Shigeru Asaba, Why Do Firms Imitate Each Other, 31 *Acad. Mgmt. Rev.* 366, 367 (2006) (imitation of rivals is a "fundamental part of the competitive process"); *see also* Brief of *Amici Curiae* Economists in Support of Petitioners at 14-15, *Twombly*, 550 U.S. 544 (No. 05-1126). It is therefore not surprising to find, in the case at hand, that rivals in an industry built entirely on the fruits of "creative labor" tend to adopt similar safeguards to protect intellectual property. *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 156 (1975).

Conscious of these economic realities, the Court in *Twombly* set forth a standard designed to weed out deficient complaints built on allegations just as easily explained by "rational and competitive business strategy unilaterally prompted by common perceptions of the market." 550 U.S. at 554. The decision below dramatically undercuts *Twombly*, however, by instructing district courts to allow Sherman Act conspiracy claims to proceed even if the plaintiffs *fail* to allege facts that tend to rule out free-market explanations for the alleged parallel behavior.

*Twombly* struck the proper balance between giving plaintiffs the latitude to pursue plausible antitrust claims and protecting defendants from protracted litigation based on lawful, free-market conduct. The decision below upsets that balance. If left intact, it could permit plaintiffs armed with barebones complaints to impose onerous antitrust litigation costs on defendants, undoing the benefits of *Twombly* and *Iqbal* and punishing corporations for engaging in exactly what the law is designed to encourage—robust competition.

## CONCLUSION

The petition for a writ of certiorari should be granted. The Court may wish to consider summary reversal.

Respectfully submitted.

THOMAS G. HUNGAR
*Counsel of Record*
JOSEPH KATTAN, PC
THOMAS M. JOHNSON, JR.
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 955-8500

August 20, 2010

# APPENDIX

## APPENDIX A

**Kevin STARR, Matt Putman, Cindy Seley, on behalf of herself and all others similarly situated, David Paschkett, on behalf of all others similarly situated, Christopher Michaud, on behalf of himself and all others similarly situated, Lisa Owens, Richard Benham, on behalf of himself and all others similarly situated, Keaton Landry, individually and on behalf of all others similarly situated, Sheri Clark, Rachael Hall and Mitchell Horton, Plaintiffs–Appellants,**

v.

**SONY BMG MUSIC ENTERTAINMENT, Sony Corporation of America, Bertelsmann, Inc., Universal Music Group, Time Warner Inc., formerly known as AOL Time Warner Cable, Inc., Warner Music Group Corp., EMI Music North America, Capitol Records Inc., doing business as EMI Music North America, John Does 1–100, Bertelsmann Music Group, Inc., BMG Music, BMG Music Publishing, doing business as the RCA Record Label, Capitol–EMI Music, Inc. and Virgin Records America, Inc., Defendants–Appellees.***

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* The Clerk of the Court is directed to amend the official caption as set forth above.

**Docket No. 08-5637-cv**

United States Court of Appeals,
Second Circuit,

Argued: Sept. 21, 2009.

Decided: Jan. 13, 2010.

Gary S. Jacobson (Christopher Lovell, Imtiaz A. Siddiqui, of counsel), Lovell Stewart Halebian LLP, New York, NY; John Stoia and Bonny Sweeney, of counsel, Coughlin Stoia Geller Rudman & Robbins LLP, San Diego, CA, for Plaintiffs–Appellants.

Kenneth R. Logan (Helena Almeida, of counsel), Simpson Thatcher & Bartlett LLP, New York, NY; Alan M. Wiseman, Mark C. Schechter, and Thomas A. Isaacson, of counsel, Howrey LLP, Washington, DC; Peter T. Barbur and Rachel G. Skaistis, of counsel, Cravath, Swaine & Moore LLP, New York, NY, for Defendants–Appellees.

Before: NEWMAN, WALKER, and KATZMANN, Circuit Judges.

KATZMANN, Circuit Judge:

This case calls upon us to determine whether an antitrust complaint alleging a conspiracy by major record labels to fix the prices and terms under which their music would be sold over the Internet states a claim for violation of Section 1 of the Sherman Act under *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007). We hold that Plaintiffs-Appellants' Second Consolidated Amended Complaint ("SCAC") contains "enough factual matter (taken as true) to suggest that an agreement was made," *id.* at 555, 127 S.Ct. 1955, and therefore states a claim. We vacate the judg-

ment of the district court and remand for further proceedings consistent with this opinion.

## BACKGROUND

The SCAC contains the following non-conclusory factual allegations, which we must accept as true.[1]

Defendants produce, license and distribute music sold as digital files ("Digital Music") online via the Internet ("Internet Music") and on compact discs ("CDs"). Together, defendants EMI, Sony BMG Music Entertainment ("Sony BMG"), Universal Music Group Recordings, Inc. ("UMG"), and Warner Music Group Corp. ("WMG"), control over 80% of Digital Music sold to end purchasers in the United States.

Initially, defendants Bertelsmann, Inc. ("Bertelsmann"), WMG, and EMI agreed to launch a service called MusicNet. Defendants UMG and Sony Corporation ("Sony") agreed to launch a service called Duet, later renamed pressplay. All defendants signed distribution agreements with MusicNet or pressplay and sold music directly to consumers over the Internet through these ventures (the "joint ventures"). Both the joint ventures and the Recording

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[1] The Supreme Court's most recent iteration of the Federal Rules of Civil Procedure Rule 8(a) pleading standard stresses that "the tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions. . . . [Therefore,] a court considering a motion to dismiss can choose to begin by identifying pleadings that, because they are no more than conclusions, are not entitled to the assumption of truth." *Ashcroft v. Iqbal*, ___ U.S. ___, 129 S.Ct. 1937, 1949–50, 173 L.Ed.2d 868 (May 18, 2009). We accept that invitation here, and do not include those allegations in the SCAC that "are no more than conclusions."

Industry Association of America ("RIAA") provided a forum and means through which defendants could communicate about pricing, terms, and use restrictions.

To obtain Internet Music from all major record labels, a consumer initially would have had to subscribe to both MusicNet and pressplay, at a cost of approximately $240 per year. Both services required consumers to agree to unpopular Digital Rights Management terms ("DRMs"). For example, pressplay prohibited consumers from copying more than two songs from any particular artist onto a CD each month. Music purchased from MusicNet and pressplay would often "expire" unless repurchased: A MusicNet consumer would need to repurchase music each year and a pressplay consumer who unsubscribed would immediately lose access to all of the music he or she had purchased. MusicNet and pressplay also did not allow consumers to transfer songs from their computers to portable digital music players like the iPod. One industry commentator observed that MusicNet and pressplay did not offer reasonable prices, and one prominent computer industry magazine concluded that "nobody in their right mind will want to use" these services. SCAC ¶ 77.

Moreover, the pricing of CDs accounted for costs such as copying the compact discs; producing the CD case, labels and anti-shoplifting packaging; shipping, both to the distributor and then to record stores; labor, such as shelving CDs and staffing cash registers; and damaged and unsold inventory. All of these costs were eliminated with Internet Music. SCAC ¶ 71. However, these dramatic cost reductions were not accompanied by dramatic price reductions for

Internet Music, as would be expected in a competitive market.

Eventually, defendants and the joint ventures began to sell Internet Music to consumers through entities they did not own or control. However, the entities could only sell defendants' music if they contracted with MusicNet to provide Internet Music for the same prices and with the same restrictions as MusicNet itself or other MusicNet licensees. If the licensee attempted to license music from another company, defendants forced them to pay penalties or terminated their licenses. In addition, each defendant was paid shares of the total revenue generated by a joint venture licensee, rather than on a per song basis, linking each defendant's financial interest in the joint venture to the total sales of all labels rather than to its own market share.

Defendants also used Most Favored Nation clauses ("MFNs") in their licenses that had the effect of guaranteeing that the licensor who signed the clause received terms no less favorable than the terms offered to other licensors. Defendants attempted to hide the MFNs because they knew they would attract antitrust scrutiny. For example, EMI and MusicNet had a "side letter" agreement which assured that EMI's core terms would be no less favorable than Bertelsmann's and WMG's. "EMI CEO Rob Glaser decided to put the MFN in a secret side letter because 'there are legal/antitrust reasons why it would be bad idea to have MFN clauses in any, or certainly all, of these agreements.'" SCAC ¶ 95. UMG also used MFN clauses in its license agreements. A January 12, 2006 article in the Wall Street Journal confirmed that defendants used MFNs, and, according to Jonathan Potter, the executive director

of the Digital Music Association, "seller-side MFNs are inherently price-increasing and anticompetitive." SCAC ¶ 97.

Edgar Bronfman, Jr., the current CEO of WMG, explained pressplay's pricing scheme as follows:

> Pressplay has what we call an affiliate model where we determine the price, and we offer a percentage of that price to the retailing partner. . . . The reason we've chosen that, frankly, is because we are concerned that the continuing devaluation of music will proceed unabated unless we do something about it.

SCAC ¶ 86.

After services other than defendants' joint ventures began to distribute defendants' Internet Music, defendants "agreed"[2] to a wholesale price floor of about 70 cents per song, which they enforced in part through MFN agreements. The MFN agreements, signed by Internet Music retailers and defendants, specified that the retailers had to pay each defendant the same amount per song. Whereas eMusic, the most popular online music service selling Internet Music owned by independent labels, currently charges $0.25 per song and places no restrictions on how purchasers can upload their music to digital music players (like the iPod) or burn to CDs, defendants' wholesale price is more than double, about $0.70 per song. Moreover, all defendants refuse to do business with eMusic, the # 2 Internet Music retailer behind only the iTunes Store.

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[2] The allegation that defendants agreed to this price floor is obviously conclusory, and is not accepted as true.

Finally, the SCAC alleges that defendants' price fixing is currently the subject of: 1) a pending investigation by the Office of the New York State Attorney General regarding wholesale prices charged for Internet Music; 2) a Department of Justice ("DOJ") investigation into collusion and price fixing begun in March 2006; and 3) a DOJ investigation into whether defendants misled DOJ about the formation and operation of MusicNet and pressplay.

Based on all of these factual allegations, plaintiffs allege that defendants engaged in a continuing conspiracy to "restrain the availability and distribution of Internet Music, fix and maintain at artificially high and non-competitive levels the prices at which they sold Internet Music and impose unreasonably restrictive terms in the purchase and use of Internet Music." SCAC ¶ 126. They also allege that they were injured by paying more for Internet Music and CDs than they would have in the absence of an illegal agreement.

From December 29, 2005 through July 2006, plaintiffs filed actions in various state and federal courts, alleging defendants had agreed to fix the price of Digital Music. The Judicial Panel on Multidistrict Litigation transferred and centralized twenty-eight actions to the Southern District of New York, before Judge Loretta Preska. In April 2007, plaintiffs filed a First Consolidated Amended Complaint. Pursuant to the district court's orders, defendants then provided plaintiffs with a letter summarizing the grounds on which they intended to move to dismiss the First Consolidated Amended Complaint. Plaintiffs filed a Second Consolidated Amended Complaint ("SCAC") in June 2007. The SCAC brought claims under Section 1 of the Sherman Act

and state antitrust and unfair and deceptive trade practices statutes. It also brought state common law claims for unjust enrichment. On July 30, 2007 defendants moved to dismiss the SCAC, pursuant to Federal Rule of Civil Procedure 12(b)(6).

At oral argument, plaintiffs requested leave to amend paragraph ninety-nine of the SCAC to allege a parallel price increase. The proposed amendment alleged that:

> By early 2005, Defendants Sony BMG's, Capitol–EMI Music's, UMG's and WMG's direct costs had gone substantially down because each of these Defendants' digitization costs of the initial cataloging had been completed, technological improvements (including increased computer processing power and speed) had reduced the remaining costs of digitizing new releases, the return and store credit and other costs alleged in ¶ 71 remained at zero or virtually zero despite substantially higher sales volumes, and the fixed costs of each of these Defendants' digital business per unit of sales volume had declined by approximately two-thirds. Nonetheless, these Defendants then engaged in or about May 2005 in the parallel, highly unusual behavior of each raising prices from the 65 cents per song level to at or about 70 cents per song. . . .
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> These parallel, highly unusual increases in prices when direct costs had substantially decreased, enforced by MFNs, were similar to Defendants' causing, as alleged in ¶¶ 74–75, the joint ventures, via MFNs and other means, to increase the prices of Internet Mu-

> sic during 2002 to 2003 to unreasonably high levels despite substantial reductions in the direct costs of Internet Music relative to CDs.

Third Consolidated Amendment Complaint ¶ 99.

By Memorandum and Order dated October 9, 2008, the district court granted the defendants' motion to dismiss, holding that the complaint did not state a claim under *Bell Atlantic Corp. v. Twombly*. The district court first found that plaintiffs did not challenge the existence or creation of the joint ventures, and the operation of the joint ventures therefore did not yield an inference of illegal agreement. At the same time, the district court held that plaintiffs' "bald allegation that the joint ventures were shams is conclusory and implausible." *In re Digital Music Antitrust Litig.*, 592 F.Supp.2d 435, 442 (S.D.N.Y. 2008). According to the district court, plaintiffs did not challenge the joint ventures' "explicit agreement," and any inference "of subsequent agreement based on prior, unchallenged explicit agreement is unreasonable." *Id.* at 443. The district court went on to hold that other circumstances alleged by plaintiffs were "equivocal" and did not justify the inference of agreement, and the imposition of the unpopular DRMs and pricing structure was not against defendants' individual economic self-interest when viewed against the backdrop of widespread music piracy. *Id.* at 444–45. Finally, the district court denied plaintiffs' motion to amend paragraph ninety-nine of the SCAC as futile. *Id.* at 445 n. 14. This appeal followed.

## DISCUSSION

We review *de novo* a district court's dismissal of a complaint for failure to state a claim under Federal Rules of Civil Procedure Rule 12(b)(6), accepting all

factual allegations as true, but "giving no effect to legal conclusions couched as factual allegations." *Port Dock & Stone Corp. v. Oldcastle Northeast, Inc.*, 507 F.3d 117, 121 (2d Cir. 2007). We review the denial of leave to amend a complaint for abuse of discretion, unless the denial was based on an interpretation of law, in which case the legal conclusion is reviewed *de novo*. *Jones v. N.Y. State Div. of Military and Naval Affairs*, 166 F.3d 45, 49 (2d Cir. 1999).

Generally, "[w]hile a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff's obligation to provide the grounds of his entitle[ment] to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." *Twombly*, 550 U.S. at 555, 127 S.Ct. 1955 (internal quotation marks omitted) (alteration in original) (citations omitted). Instead, "[f]actual allegations must be enough to raise a right to relief above the speculative level, on the assumption that all the allegations in the complaint are true (even if doubtful in fact)." *Id.* (citations omitted). What is required are "enough facts to state a claim to relief that is plausible on its face." *Id.* at 570, 127 S.Ct. 1955. In the words of the Supreme Court's most recent iteration of this standard, "[a] claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Ashcroft v. Iqbal*, ___ U.S. ___, 129 S.Ct. 1937, 1949, 173 L.Ed.2d 868 (2009). "[W]here the well-pleaded facts do not permit the court to infer more than the mere possibility of misconduct," however, dismissal is appropriate. *Id.* at 1950.

Under Section 1 of the Sherman Act, "[e]very contract, combination . . ., or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is . . . illegal." 15 U.S.C. § 1. The crucial question in a Section 1 case is therefore whether the challenged conduct "stem[s] from independent decision or from an agreement, tacit or express." *Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 540, 74 S.Ct. 257, 98 L.Ed. 273 (1954). Although parallel business behavior "is admissible circumstantial evidence from which the fact finder may infer agreement," it does not itself constitute a violation of the Sherman Act, because it is "consistent with conspiracy, but just as much in line with a wide swath of rational and competitive business strategy unilaterally prompted by common perceptions of the market." *Twombly*, 550 U.S. at 553–54, 127 S.Ct. 1955 (internal quotation marks omitted).

While for purposes of a summary judgment motion, a Section 1 plaintiff must offer evidence that "tend[s] to rule out the possibility that the defendants were acting independently," *id.* at 554, 127 S.Ct. 1955 (citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986)), to survive a motion to dismiss under Rule 12(b)(6), a plaintiff need only allege "enough factual matter (taken as true) to suggest that an agreement was made." *Id.* at 556, 127 S.Ct. 1955; *see also In re Elevator Antitrust Litig.*, 502 F.3d 47, 50 (2d Cir. 2007) (per curiam) (quoting *Twombly* for the same proposition).

As the Supreme Court clarified in *Twombly*:

> Asking for plausible grounds to infer an agreement does not impose a probability re-

> quirement at the pleading stage; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement. And, of course, a well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and that a recovery is very remote and unlikely.

*Id.* at 556, 127 S.Ct. 1955 (footnote and internal quotation marks omitted).

Thus, an allegation of parallel conduct coupled with only a bare assertion of conspiracy is not sufficient to state a Section 1 claim. *Id.* Instead, allegations of parallel conduct "must be placed in a context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action." *Id.* at 557, 127 S.Ct. 1955. Examples of a parallel conduct allegation that would suffice under this standard include "parallel behavior that would probably not result from chance, coincidence, independent responses to common stimuli, or mere interdependence unaided by an advance understanding among the parties." *Id.* at 556 n. 4, 127 S.Ct. 1955 (internal quotation marks omitted).

In *Twombly*, plaintiffs brought a Section 1 claim centered around the market for local telephone service. In 1984, a system of seven regional local-telephone-service monopolies, called Baby Bells, was created, along with a separate, competitive market for long-distance telephone service from which the regional Baby Bells were excluded. *Id.* at 549, 127 S.Ct. 1955. In 1996, Congress withdrew approval for the regional Baby Bell monopolies in enacting the Telecommunications Act of 1996, which required the Baby Bells to share their local networks with com-

petitors (called "CLECs"), in exchange for authority to enter the long-distance service market. *Id.* Not surprisingly, the Baby Bells vigorously litigated their "sharing" obligations under the Act. *Id.* Not satisfied with the Baby Bells' efforts at sharing, the plaintiffs in *Twombly* sued, alleging that the Baby Bells engaged in parallel conduct in their respective regions, including making unfair agreements with the CLECs for access to Baby Bell networks, providing CLECs inferior connections to those networks, and overcharging the CLECs, all in order to inhibit the growth of CLECs and prevent them from competing effectively with the Baby Bells. *Id.* at 550–51, 127 S.Ct. 1955. The complaint also alleged that the Baby Bells' failure to compete with one another, coupled with a statement from one Baby Bell's CEO that competing in the territory of another Baby Bell "might be a good way to turn a quick dollar but that doesn't make it right," supported the allegation that the Baby Bells entered into a conspiracy to prevent entry into their local markets and agreed to refrain from competing with one another. *Id.* at 551, 127 S.Ct. 1955.

The Supreme Court held that the ultimate conspiracy allegation was merely a "legal conclusion[ ] resting on the prior allegations," *id.* at 564, 127 S.Ct. 1955, and the actual factual allegations in the complaint were insufficient because they did not "invest[ ] either the action or inaction alleged with a plausible suggestion of conspiracy." *Id.* at 566, 127 S.Ct. 1955. It was natural for each Baby Bell to resist the competition from the CLECs that the 1996 Act mandated, and "nothing in the complaint intimates that the resistance to the [CLECs] was anything more than the natural, unilateral reaction of each [Baby Bell] intent on keeping its regional domi-

nance." *Id.* at 566, 127 S.Ct. 1955. As to the Baby Bells' failure to encroach on each others' territory, given that prior to the Telecommunications Act of 1996 monopoly was the norm, rather than the exception, "a natural explanation for the noncompetition alleged is that the former Government-sanctioned monopolists were sitting tight, expecting their neighbors to do the same. . . . [T]he complaint itself [gave] reasons to believe that the [Baby Bells] would see their best interests in keeping to their old turf." *Id.* at 568, 127 S.Ct. 1955.

Applying the language and reasoning of *Twombly* to the facts of this case leads us to conclude respectfully that the district court erred in dismissing the complaint for failure to state a Section 1 claim. The present complaint succeeds where *Twombly*'s failed because the complaint alleges specific facts sufficient to plausibly suggest that the parallel conduct alleged was the result of an agreement among the defendants. As discussed above, the complaint contains the following non-conclusory factual allegations of parallel conduct. First, defendants agreed to launch MusicNet and pressplay, both of which charged unreasonably high prices and contained similar DRMs. Second, none of the defendants dramatically reduced their prices for Internet Music (as compared to CDs), despite the fact that all defendants experienced dramatic cost reductions in producing Internet Music. Third, when defendants began to sell Internet Music through entities they did not own or control, they maintained the same unreasonably high prices and DRMs as MusicNet itself. Fourth, defendants used MFNs in their licenses that had the effect of guaranteeing that the licensor who signed the MFN received terms no less favorable than terms offered to other licensors. For example,

both EMI and UMG used MFN clauses in their licensing agreements with MusicNet. Fifth, defendants used the MFNs to enforce a wholesale price floor of about 70 cents per song. Sixth, all defendants refuse to do business with eMusic, the # 2 Internet Music retailer. Seventh, in or about May 2005, all defendants raised wholesale prices from about $0.65 per song to $0.70 per song. This price increase was enforced by MFNs.[3]

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[3] Because the proposed amendment to paragraph ninety-nine of the SCAC contained, along with the remainder of the complaint, "enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement," *Twombly*, 550 U.S. at 556, 127 S.Ct. 1955, the district court erred in denying the motion to amend on the ground of futility. *See Kassner v. 2nd Ave. Delicatessen Inc.*, 496 F.3d 229, 244 (2d Cir. 2007). Therefore, we include the allegations contained in proposed paragraph ninety-nine within our discussion of the SCAC as a whole. In so doing, we reject defendants' argument that the proposed amendment would have been futile because it alleged that prices rose in or about May 2005, but costs declined four years earlier, in 2001. As can be seen above, paragraph seventy-one of the original complaint alleged that initial costs of distributing Internet Music fell because the price of distributing CDs accounted for costs such as copying the compact discs, producing the CD case, and labor, all of which were eliminated in distributing Internet Music. In contrast, the proposed amendment to paragraph ninety-nine alleged that by May 2005 the costs of distributing Internet Music had fallen because the digitization costs of the initial Internet cataloging had been completed and technological improvements (including increased computer processing power) had reduced the remaining costs of digitizing new releases. These are not the same costs that are alleged to have decreased in paragraph seventy-one of the original complaint.

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More importantly, the following allegations, taken together, place the parallel conduct "in a context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action." *Twombly*, 550 U.S. at 557, 127 S.Ct. 1955. First, defendants control over 80% of Digital Music sold to end purchasers in the United States. *See* 7 Phillip E. Areeda and Herbert Hovenkamp, *Antitrust Law* (hereinafter "Areeda & Hovenkamp") § 1431a (2d ed. 2003) ("[E]mpirical studies considering many industries have suggested that noncompetitive pricing [that may be the result of price coordination] is likely to appear when the four leading firms account for some 50 to 80 percent of the market."). Second, one industry commentator noted that "nobody in their right mind" would want to use MusicNet or pressplay, suggesting that some form of agreement among defendants would have been needed to render the enterprises profitable. *See id.* § 1415b ("Some acts, or failures to act, cannot be profitably continued unless rivals behave in parallel."); *In re Flat Glass Antitrust Litig.*, 385 F.3d 350, 360–361 (3d Cir. 2004) ("Evidence that the defendant acted contrary to its interests means evidence of conduct that would be irrational assuming that the defendant operated in a competitive market. In a competitive industry, for example, a firm would cut its price with the hope of increasing its market share if its competitors were setting prices above marginal costs."). Third, the quote from Edgar Bronfman, the current CEO of WMG, suggests that pressplay was formed expressly as an effort to stop the "continuing devaluation of music."

Fourth, defendants attempted to hide their MFNs because they knew they would attract antitrust scrutiny. For example, EMI and MusicNet's

MFN, which assured that EMI's core terms would be no less favorable than Bertelsmann's or WMG's, was contained in a secret side letter. "EMI CEO Rob Glaser decided to put the MFN in a secret side letter because 'there are legal/antitrust reasons why it would be bad idea to have MFN clauses in any, or certainly all, of these agreements." SCAC ¶ 95. According to the executive director of the Digital Music Association, seller-side MFNs are "inherently price-increasing and anticompetitive." SCAC ¶ 97.

Fifth, whereas eMusic charges $0.25 per song, defendants' wholesale price is about $0.70 per song. *See* 7 Areeda & Hovenkamp § 1415b ("[O]ne cannot profitably increase its price above that charged by rivals unless they follow the price-raiser's lead."). Sixth, defendants' price-fixing is the subject of a pending investigation by the New York State Attorney General and two separate investigations by the Department of Justice. Finally, defendants raised wholesale prices from about $0.65 per song to $0.70 per song in or about May 2005, even though earlier that year defendants' costs of providing Internet Music had decreased substantially due to completion of the initial digital cataloging of all Internet Music and technological improvements that reduced the costs of digitizing new releases. *See* Richard A. Posner, *Antitrust Law* 88 (2d ed. 2001) ("Simultaneous price increases . . . unexplained by any increases in cost may therefore be good evidence of the initiation of a price-fixing scheme.").

This complaint does not resemble those our sister circuits have held fail to state a claim under *Twombly*. *See, e.g.*, *Rick–Mik Enters., Inc. v. Equilon Enters., LLC*, 532 F.3d 963, 975–976 (9th Cir. 2008) (dismissing Section 1 price fixing complaint under

*Twombly* where complaint alleged only that defendant conspired with "numerous" banks to fix the price of credit and debit card processing fees and received kickbacks from "numerous" banks as consideration for its unlawful agreement); *Kendall v. Visa U.S.A., Inc.*, 518 F.3d 1042, 1048–50 (9th Cir. 2008) (where plaintiffs alleged no facts to support their theory that defendant banks conspired or agreed with each other, dismissing Section 1 claim because plaintiffs pleaded only legal conclusions, and "failed to plead the necessary evidentiary facts to support those conclusions").

Defendants' arguments that plaintiffs have failed to state a claim are without merit. Defendants first argue that a plaintiff seeking damages under Section 1 of the Sherman act must allege facts that "tend[ ] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior." Appellee's Br. 15–17. This is incorrect. Although the *Twombly* court acknowledged that for purposes of summary judgment a plaintiff must present evidence that tends to exclude the possibility of independent action, 550 U.S. at 554, 127 S.Ct. 1955, and that the district court below had held that plaintiffs must allege additional facts that tended to exclude independent self-interested conduct, *id.* at 552, 127 S.Ct. 1955, it specifically held that, to survive a motion to dismiss, plaintiffs need only "enough factual matter (taken as true) to suggest that an agreement was made," *id.* at 556, 127 S.Ct. 1955; *see also* 2 Areeda & Hovenkamp § 307d1 (3d ed. 2007) ("[T]he Supreme Court did *not* hold that the same standard applies to a complaint and a discovery record. . . . The 'plausibly suggesting' threshold for a conspiracy complaint remains considerably less than the 'tends to rule out the possibility' standard for summary judgment.").

Defendants next argue that *Twombly* requires that a plaintiff identify the specific time, place, or person related to each conspiracy allegation. This is also incorrect. The *Twombly* court noted, in dicta, that had the claim of agreement in that case not rested on the parallel conduct described in the complaint, "we doubt that the . . . references to an agreement among the [Baby Bells] would have given the notice required by Rule 8 . . . [because] the pleadings mentioned no specific time, place, or person involved in the alleged conspiracies." 550 at 565 n. 10. In this case, as in *Twombly*, the claim of agreement rests on the parallel conduct described in the complaint. Therefore, plaintiffs were not required to mention a specific time, place or person involved in each conspiracy allegation.

Defendants then argue that inferring a conspiracy from the facts alleged is unreasonable because plaintiffs' allegations "are the very same claims that were thoroughly investigated and rejected by the Antitrust Division of the Department of Justice," Appellee's Br. 17–18, which closed its inquiry in December 2003 and publicly announced that it had uncovered no evidence that the joint ventures had harmed competition or consumers of digital music. Even if we could consider this evidence on a motion to dismiss, defendants cite no case to support the proposition that a civil antitrust complaint must be dismissed because an investigation undertaken by the Department of Justice found no evidence of conspiracy. Second, this argument neglects the fact that the complaint alleges that the Department of Justice has, since 2003, launched two new investigations into whether defendants engaged in collusion and price fixing and whether defendants misled the Depart-

ment about the formation and operation of MusicNet and pressplay.

The only one of defendants' contentions that merits more than a brief discussion is the impact of the Supreme Court's decision in *Texaco Inc. v. Dagher*, 547 U.S. 1, 126 S.Ct. 1276, 164 L.Ed.2d 1 (2006). That case concerned a joint venture formed by Texaco and Shell Oil to completely consolidate their operations in the western United States. The joint venture, Equilon, produced significant cost savings in production and marketing, *see Dagher v. Saudi Refining, Inc.*, 369 F.3d 1108, 1111 (9th Cir. 2004), *rev'd*, 547 U.S. 1, 126 S.Ct. 1276, 164 L.Ed.2d 1 (2006), and ended competition between Texaco and Shell Oil altogether in the domestic refining and selling of gasoline. Because Texaco and Shell Oil's market share exceeded twenty-five percent, *id.*, the formation of Equilon was approved by consent decree by the Federal Trade Commission, as well as by state attorneys general in California, Hawaii, Oregon, and Washington. *Dagher*, 547 U.S. at 4, 126 S.Ct. 1276. Plaintiffs sued, alleging that in allowing Equilon to determine the price of gasoline, Texaco and Shell Oil violated the per se rule against price fixing under § 1 of the Sherman Act. The district court granted summary judgment to Texaco and Shell Oil, holding that the rule of reason, rather than a *per se* rule, governed the claim, and because plaintiffs eschewed the rule of reason analysis, judgment was appropriate as a matter of law. *Id.*[4] The Supreme Court agreed, holding

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[4] A short explanation of *per se* illegality versus the rule of reason is in order. *Per se* liability is reserved "for only those agreements that are so plainly anticompetitive that no elabo-

[Footnote continued on next page]

that Equilon's pricing policy was not a price-fixing agreement between competitors, because Texaco and Shell Oil did not compete with one another in the relevant market (the sale of gasoline). Therefore, the *per se* rule against price fixing did not apply. *Id.* at 5–6. In its holding, the Supreme Court presumed that Equilon was a lawful joint venture, because its formation had been approved by federal and state regulators and plaintiffs did not argue that it was a sham. *Id.* at 6 n. 1. Finally, the Supreme Court noted that despite the lawfulness of the joint venture plaintiffs could have, but did not, challenge Equilon's pricing policy under the rule of reason. *Id.* at 7.

*Dagher* does not support the dismissal of the complaint in this case. First, although the district court below stated that plaintiffs did not challenge the joint ventures here, the complaint makes clear that plaintiffs do challenge the joint ventures. *See, e.g.*, SCAC ¶¶ 67, 72–73, 76, 78, 81–83, 85. In the legal memorandum relied upon by the district court for the proposition that plaintiffs did not challenge the joint ventures, plaintiffs wrote that while "it is

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[Footnote continued from previous page]

rate study of the industry is needed to establish their illegality." *Dagher*, 547 U.S. at 5, 126 S.Ct. 1276 (internal quotation marks omitted). Price-fixing agreements between competitors are generally *per se* unlawful, meaning they are prohibited despite the reasonableness of the particular prices agreed upon. *Id*; *see also* 7 Areeda & Hovenkamp § 1509a (2d ed.2003). In contrast, under the rule of reason analysis, which presumptively applies to Section 1 claims, "antitrust plaintiffs must demonstrate that a particular contract or combination is in fact unreasonable and anticompetitive before it will be found unlawful." *Dagher*, 547 U.S. at 5, 126 S.Ct. 1276.

not the existence or creation of these joint ventures that form the basis of the [p]laintiffs' allegations," defendants used the joint ventures "as a means to implement their anticompetitive agreements" and to "facilitat[e] anticompetitive . . . horizontal combinations." *See* Pls.' Consolidated Mem. of Law in Opp'n to Defs.' Supplemental Mem. of Law 10–11. The memorandum also called MusicNet and pressplay "mere puppets of [the] [d]efendants." *See id.* at 11. The district court implicitly acknowledged that plaintiffs did challenge the joint ventures when it held that plaintiffs' allegation that the joint ventures were shams was conclusory and implausible. Plaintiffs continue to challenge the joint ventures on appeal, and defendants do not contend that MusicNet or pressplay were explicitly approved by state or federal regulators. Therefore, the *Dagher* Court's presumption that Equilon was lawful because its formation had been approved by federal and state regulators and plaintiffs did not argue that it was a sham, 547 U.S. at 6 n. 1, 126 S.Ct. 1276, is not applicable here.[5] Second, even if we were to presume that Mu-

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[5] We note that some commentators continue to believe that Dagher does not foreclose the application of the per se rule against price-fixing in the case of a lawful joint venture where the price fixing itself is not related to the purpose of the joint venture or the joint venture does not result in significant economic benefits. *See* Areeda & Hovenkamp 2009 Supplement § 2132 (arguing that if General Motors and Toyota were to form a joint venture for the production of hybrid car engines, but then place the engines in cars they designed and produced separately, the Supreme Court would not permit them to fix the prices of the finished cars as part of the lawful joint venture); *see also* 12 Areeda & Hovemkamp § 2004a (2d ed.2005) (noting that the *per se* rule against price fixing "applies virtually with-

[Footnote continued on next page]

sicNet and pressplay were lawful, which we do not, plaintiffs would still be free to challenge their activities pursuant to the rule of reason. *Dagher*, 547 U.S. at 6 n. 1, 126 S.Ct. 1276. The complaint alleges that the activities of the joint ventures actually were anticompetitive and unreasonable, SCAC ¶ 126, and, unlike in *Dagher*, plaintiffs in this case have not "eschewed" a rule of reason analysis. Similarly, the complaint contains many allegations of conduct that took place outside of the joint ventures, and are therefore not affected by *Dagher*. For all of these reasons, *Dagher* does not support dismissal of the SCAC.

Finally, defendants claim that the conduct alleged in the complaint "would be entirely consistent with independent, though parallel, action." Appellee's Br. 20. Under *Twombly*, allegations of parallel conduct that could "just as well be independent ac-

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[Footnote continued from previous page]

out exception when the price fix is 'naked' in the sense that it does not accompany any significant integration of research and development, production or distribution. . . . As a general matter, price fixing is tolerated only in the case of the joint venture producing significant, output-increasing efficiencies, and where the price fixing itself can be shown to be essential to these social gains."); 11 Areeda & Hovenkamp § 1912c (2d ed.2005) (explaining that the rule of reason is applied to a joint venture's horizontal restraint when the joint venture seems to be productive or reasonable on its face and the particular challenged agreement seems to be reasonably necessary to the purpose of the venture). In this case, the SCAC obviously does not allege that MusicNet or pressplay were economically efficient in integrating research, development, production, or distribution or that price fixing was reasonably necessary to any social gain the ventures may have produced.

tion" are not sufficient to state a claim. 550 U.S. at 557, 127 S.Ct. 1955. However, in this case plaintiffs have alleged behavior that would plausibly contravene each defendant's self-interest "in the absence of similar behavior by rivals." 7 Areeda & Hovenkamp § 1415a (2d ed.2003); *see also* Posner, *supra*, at 100. For example, it would not be in each individual defendant's self-interest to sell Internet Music at prices, and with DRMs, that were so unpopular as to ensure that "nobody in their right mind" would want to purchase the music, unless the defendant's rivals were doing the same. For these reasons we hold that the SCAC states a claim under *Twombly*.[6]

## CONCLUSION

The Second Consolidated Amendment Complaint contains "plausible grounds to infer an agreement." *Twombly*, 550 U.S. at 556, 127 S.Ct. 1955. We therefore hold that the district court erred in dismissing the complaint. The case is remanded for further proceedings consistent with this opinion.

JON O. NEWMAN, Circuit Judge, concurring:

I concur in Judge Katzmann's comprehensive opinion, but add these additional words to explore a perplexing aspect of the Supreme Court's decision in *Bell Atlantic v. Twombly*, 550 U.S. 544, 127 S.Ct.

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[6] On appeal, three parent-company defendants, Bertelsmann, Inc., Sony Corporation of America, and Time Warner Inc., argue that even if the SCAC states a claim under *Twombly*, it fails to state a claim against them because plaintiffs allege no basis for piercing the corporate veil. Because the district court did not reach this question and the parties devote three total pages to it in their briefs, we remand to allow the district court to consider it in the first instance.

1955, 167 L.Ed.2d 929 (2007). As is well known, the Court there ruled insufficient to survive a motion to dismiss a complaint that endeavored to allege a price-fixing agreement in violation of section 1 of the Sherman Act, 15 U.S.C. § 1. The complaint had relied primarily on an allegation of the defendants' parallel conduct.

The perplexing aspect of the Court's opinion is contained in the very first paragraph of the Court's substantive discussion. The Court there stated:

> While a showing of parallel "business behavior is admissible circumstantial evidence *from which the fact finder may infer agreement*," it falls short of "conclusively establish[ing] agreement or . . . itself constitut[ing] a Sherman Act offense.

*Twombly*, 550 U.S. at 553, 127 S.Ct. 1955 (emphasis added) (citing *Theatre Enterprises v. Paramount Film Distributing Corp.*, 346 U.S. 537, 540–41, 74 S.Ct. 257, 98 L.Ed. 273 (1954)) (alterations and ellipsis in original).[1]

If, as the Court states in the first part of this sentence, a fact-finder is entitled to infer agreement from parallel conduct, one may wonder why a complaint alleging such conduct does not survive a motion to dismiss. The answer is surely not supplied by

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[1] The basis for perplexity is not lessened by the Court's subsequent statement that "[i]t makes sense to say, therefore, that an allegation of parallel conduct and a bare assertion of conspiracy will not suffice," *Twombly*, 550 U.S. at 556, 127 S.Ct. 1955, apparently meaning will not suffice to defeat a motion to dismiss a complaint.

the remainder of the Court's sentence. That portion states the unexceptional proposition that parallel conduct alone is not *conclusive* evidence of an agreement to fix prices. To support that proposition, the Court cites *Theatre Enterprises*. But that case was an appeal by an antitrust plaintiff whose complaint had *survived* a motion to dismiss. Indeed, that plaintiff had been permitted to present its evidence to a jury, only to have the jury reject on the merits the claim of a section 1 violation. The plaintiff sought review on the ground that the trial court had erred in not granting a motion for a directed verdict in the plaintiff's favor. *See Theatre Enterprises*, 346 U.S. at 539, 74 S.Ct. 257. The Supreme Court understandably found no error. *See id.* at 539–42, 74 S.Ct. 257. In *Twombly*, the Court noted the extraordinary claim that the *Theatre Enterprises* plaintiff had made. "An antitrust conspiracy plaintiff with evidence showing nothing more than parallel conduct is not entitled *to a directed verdict*." *Twombly*, 550 U.S. at 554, 127 S.Ct. 1955 (emphasis added).

The fact that an allegation of parallel conduct was held insufficient to require a directed verdict in the plaintiff's favor is hardly a basis for ruling that such an allegation is insufficient to survive a motion to dismiss for failure to state a claim on which relief may be granted.

In view of the Court's initial observation in *Twombly* that parallel conduct is sufficient to support a permissible inference of an agreement, the reason for the rejection of the complaint in *Twombly* must arise from something other than the plaintiff's reliance on parallel conduct. That reason is not difficult to find. It is the *context* in which the defendants' parallel conduct occurred. "[W]hen allegations of

parallel conduct are set out in order to make a § 1 claim, they must be placed in a context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action." *Id.* at 557, 127 S.Ct. 1955.

The context in *Twombly* was the aftermath of the divestiture of AT&T's local telephone service, resulting in the creation of seven Regional Bell Operating Companies, the so-called "Baby Bells" or Incumbent Local Exchange Carriers ("ILECs"). *See id.* at 549, 127 S.Ct. 1955. Originally restricted to providing local telephone service, the ILECs were later permitted by the Telecommunications Act of 1996, Pub.L. No. 104–104, 110 Stat. 56 (Feb. 8, 1996), to enter the long-distance market upon compliance with conditions concerning the opportunity for competitive local exchange carriers ("CLECs") to make use of an ILEC's network. *See Twombly*, 550 U.S. at 549, 127 S.Ct. 1955.

In that context, it was entirely understandable for the Court to cast a jaundiced eye on the claim that the parallel conduct of these newly created ILECs would suffice to permit an inference of agreement. As the Court observed:

> [The parallel conduct of the ILECs] was not suggestive of conspiracy, not if history teaches anything. In a traditionally unregulated industry with low barriers to entry, sparse competition among large firms dominating separate geographical segments of the market could very well signify illegal agreement, but here we have an obvious alternative explanation. In the decade preceding the 1996 Act and well before that, monopoly was the norm in telecommunications, not the ex-

> ception. The ILECs were born in that world, doubtless liked the world the way it was, and surely knew the adage about him who lives by the sword. Hence, a natural explanation for the noncompetition alleged is that the former Government-sanctioned monopolists were sitting tight, expecting their neighbors to do the same thing.

*Id.* at 567–68, 127 S.Ct. 1955.

Two years after *Twombly*, the Court emphasized its view that whether a bare allegation of illegality would suffice to withstand a motion to dismiss depends on the context in which the allegation is made. "Determining whether a complaint states a plausible claim for relief will, as the Court of Appeals observed, be a context-specific task that requires the reviewing court to draw on its judicial experience and common sense." *Ashcroft v. Iqbal*, ___ U.S. ___, 129 S.Ct. 1937, 1950, 173 L.Ed.2d 868 (2009).

I believe it would be a serious mistake to think that the Court has categorically rejected the availability of an inference of an unlawful section 1 agreement from parallel conduct. Even in those contexts in which an allegation of parallel conduct will not suffice to take an antitrust plaintiff's case to the jury, it will sometimes suffice to overcome a motion to dismiss and permit some discovery, perhaps leaving the issue for later resolution on a motion for summary judgment.

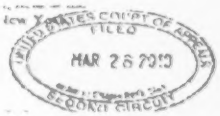
In the pending case, as Judge Katzmann has carefully demonstrated, the context in which the defendants' alleged parallel conduct occurred, amplified by specific factual allegations making plausible an inference of agreement, suffices to render the allega-

tion of a section 1 violation sufficient to withstand a motion to dismiss.

## APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the Daniel Patrick Moynihan United States Courthouse, 500 Pearl Street, in the City of New York, on the 26th day of March, two thousand and ten.




Docket No. 08-5637-cv

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KEVIN STARR, MATT PUTMAN, CINDY SELEY, on behalf of herself and all others similarly situated, DAVID PASCHKETT, on behalf of all others similarly situated, CHRISTOPHER MICHAUD, on behalf of himself and all others similarly situated, LISA OWENS, RICHARD BENHAM, on behalf of himself and all others similarly situated, KEATON LANDRY, individually and on behalf of all others similarly situated, SHERI CLARK, RACHAEL HALL and MITCHELL HORTON,

*Plaintiffs–Appellants,*

v.

SONY BMG MUSIC ENTERTAINMENT, SONY CORPORATION OF AMERICA, BERTELSMANN, INC., UNIVERSAL

MUSIC GROUP, TIME WARNER INC., formerly known as AOL Time Warner Cable, Inc., WARNER MUSIC GROUP CORP., EMI MUSIC NORTH AMERICA, CAPITOL RECORDS INC., doing business as EMI MUSIC NORTH AMERICA, JOHN DOES 1–100, BERTELSMANN MUSIC GROUP, INC., BMG MUSIC, BMG MUSIC PUBLISHING, doing business as The RCA Record Label, CAPITOL–EMI MUSIC, INC. AND VIRGIN RECORDS AMERICA, INC.,

*Defendants–Appellees.*

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SONY BMG MUSIC ENTERTAINMENT, SONY CORPORATION OF AMERICA, BERTELSMANN, INC., UNIVERSAL MUSIC GROUP, TIME WARNER INC., formerly known as AOL Time Warner Cable, Inc., WARNER MUSIC GROUP CORP., EMI MUSIC NORTH AMERICA, CAPITOL RECORDS INC., doing business as EMI MUSIC NORTH AMERICA, JOHN DOES 1–100, BERTELSMANN MUSIC GROUP, INC., BMG MUSIC, BMG MUSIC PUBLISHING, doing business as The RCA Record Label, CAPITOL–EMI MUSIC, INC. AND VIRGIN RECORDS AMERICA, INC., having filed a petition for panel rehearing, or, in the alternative, for rehearing *en banc*, and the panel that determined the appeal having considered the request for rehearing *en banc*.

IT IS HEREBY ORDERED that the petition is denied.

FOR THE COURT:
Catherine O'Hagan Wolfe, Clerk
/s/

## APPENDIX C

**In Re: DIGITAL MUSIC ANTITRUST LITIGATION.**
**This Document Relates to: All Actions.**
**No. 06 MDL No. 1780 (LAP).**

United States District Court,
S.D. New York.
Oct. 9, 2008.

***OPINION***

LORETTA A. PRESKA, J.

This multidistrict litigation involves allegations that Bertelsmann, Inc., SONY BMG Music Entertainment, Sony Corporation of America, Capitol Records, Inc. dba EMI Music North America, EMI Group North America, Inc., Capitol–EMI Music, Inc., Virgin Records America, Inc., Time Warner Inc., UMG Recordings, Inc., and Warner Music Group Corp. (collectively, "Defendants") conspired to fix or maintain artificially the prices of Digital Music. Plaintiffs are fifteen individuals (collectively, "Plaintiffs") from nine states who seek to represent a putative nation-wide class of purchasers of Digital Music. Defendants move [dkt. no. 75] to dismiss the Second Consolidated Amended Complaint ("SCAC") under Rule 12(b)(6) of the Federal Rules of Civil Procedure

and, in the alternative, to strike certain portions of the SCAC pursuant to Rule 12(f).[1] Plaintiffs move [dkt. no. 104] to amend one paragraph of the SCAC to add certain allegations.[2] For the reasons that follow, Defendants' motion is GRANTED, and Plaintiffs' motion is DENIED.

I. *BACKGROUND*

According to the SCAC, Digital Music is music that is manufactured as a digital file. (*See* SCAC ¶ 2, In re Digital Music, 06 MDL. 1780 (filed June 13, 2007) (hereinafter "SCAC").) It is delivered in two allegedly interchangeable formats: on compact discs ("CDs") and through the internet ("Internet Music"). (*See id.* ¶ 41.) The SCAC defines the relevant market in this action as the market for sales of all Digital Music (both CDs and Internet Music) in the

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[1] The parties have submitted the following briefs in connection with Defendants' motion to dismiss: Defendants' Joint Memorandum of Law in Support of Motion to Dismiss and to Strike Portions of Plaintiffs' Second Consolidated Amended Complaint ("Defs.' Mem."); Plaintiffs' Memorandum of Law in Opposition to Defendants' Motion to Dismiss and to Strike Portions of Plaintiffs' Second Consolidated Amended Complaint ("Pls.' Opp'n"); and Defendants' Reply Memorandum of Law in Further Support of Motion to Dismiss and to Strike Portions of Plaintiffs' Second Consolidated Amended Complaint ("Defs.' Reply").

[2] The parties have submitted the following briefs in connection with Plaintiffs' motion to amend: Plaintiffs' Memorandum of Law in Support of Their Motion for Leave to Amend Paragraph 99 of the Complaint ("Pls.' ¶ 99 Mem."), and Defendants' Memorandum of Law in Opposition to Plaintiffs' Motion to Amend Paragraph Ninety–Nine (99) of the Second Consolidated Amended Complaint ("Defs.' ¶ 99 Opp'n").

United States; Defendants, described as the four largest record companies in the United States, allegedly control in excess of 80% of that market. (*See id.* ¶ 40.)

In general, the SCAC alleges that Defendants conspired to inflate and maintain at supracompetitive levels the price of Digital Music. (*See id.* ¶ 126.) They achieved this by fixing a high price for and restraining the availability of Internet Music (*id.* ¶ 66), which, in turn, buoyed the price of CDs "despite declining costs of production associated with the introduction of new technologies" (*id.* ¶ 126; *see also id.* ¶ 105). Explains the SCAC: "[a]cting alone, no defendant could sustain the supracompetitive prices for CDs prevailing in the market. This inability to charge high CD prices, as market factors made consumer demand for CDs more elastic over time at the prices charged by Defendants during the conspiracy, gave Defendants motive to conspire." (*Id.* ¶ 83.)

Defendants' manipulation of the market for Internet Music is described in two phases of conduct. The first phase centers on two joint ventures—"MusicNet" and "pressplay"—created by Defendants to distribute their Internet Music. (*Id.* ¶ 67.)[3] The second phase alleges manipulation through Defendants' business dealings with third-party licensees. (*Id.* ¶ 99.)

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[3] The SCAC alleges that Defendants Bertelsmann, WMG and EMI launched MusicNet, while UMG and Sony launched "pressplay," originally called "Duet." (SCAC ¶¶ 67, 72.)

A. *The First Phase: The Joint Ventures*

The SCAC appears to include principally two allegations concerning the joint ventures. First, it alleges that the joint ventures directly restricted the wide-spread distribution and use of Internet Music by charging supracompetitive prices and imposing unpopular digital rights management ("DRM") rules on the Internet Music they sold to consumers. (*Id.* ¶¶ 75–78; *see id.* ¶ 81 ("Defendants collectively refused to utilize or license a system that was convenient, not burdened with use restrictions and competitively priced.").)[4] According to the SCAC, Defendants enforced those price and use restrictions through their use of most-favored nations clauses ("MFNs") and "side agreements," where-under each Defendant would license its songs to the joint ventures at a price not lower than the price secured by any other Defendant. (*Id.* ¶¶ 92–94, 96–97.)[5] Thus, "Defendants' collusion in setting high prices for Internet Music, as well as their collusion in imposing unfair and one-sided terms on its use, made Internet

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[4] "Digital rights management" refers to the restrictions on a consumer's use of Internet Music. (*See* SCAC ¶ 75.) The SCAC also notes that the joint ventures allowed Defendants "to engage in the anticompetitive practice of tying or 'bundling' Internet Music onto a single online 'album.' " (*Id.* ¶ 84.)

[5] The SCAC alleges that, at the same time Defendants licensed their music to the joint ventures, they also licensed it to third-party vendors. The SCAC notes that Defendants also enforced their agreement during the joint venture phase by imposing the same price and use restrictions on the third party licensees and, further, by penalizing such licensees with higher prices or license termination if they dealt with other record labels. (*Id.* ¶ 79.)

Music less attractive to consumers, allowing Defendants to sell CDs at supracompetitive prices." (*Id.* ¶ 82.)

Second, the SCAC alleges that the joint ventures were shams that were designed solely to "provide[ ] Defendants with opportunities and forums to meet and further conspire to cooperate to maintain the prices and terms for Internet Music." (*Id.* ¶ 87.) This follows, alleges the SCAC, from the fact that certain aspects of the joint ventures' business model were contrary to the economic self-interests of each individual Defendant. Thus, "[a]ny one of the Defendants might have removed these unpopular DRM and gained additional market share and profits and most or all would have but for the conspiracy, just as independent labels not party to the conspiracy sell DRM-free Internet Music." (*Id.* ¶ 76; *see also id.* ¶ 78 ("[R]ather than pursue their individual interests by competing with each other, the new method of distribution was used as a pretext for Defendants to meet and conspire.").) Plaintiffs allege that the same was true of the way Defendants structured their compensation from the joint ventures: because Defendants were not paid on a per-song basis, their "economic incentives were to charge monopoly prices for Internet Music rather than compete with one another on price." (*Id.* ¶ 89.) Thus, instead of legitimate business entities, the joint ventures were merely "vehicles through which the Defendants effectively exchanged price information, policed their cartel and

imposed restrictive licensing arrangements that retarded the growth of Internet Music." (*Id.* ¶ 98.)[6]

The SCAC further alleges that Defendants attempted to conceal many of the joint ventures' allegedly anticompetitive practices. (*Id.* ¶ 113.) For instance, Defendants—through the joint ventures—allegedly "conspired to mask their anticompetitive conduct by pretextually establishing rules to prevent antitrust violations, ignoring them, and then using these sham rules to convince the United States Department of Justice [("DOJ")] to drop the investigation it launched in 2001." (*Id.* ¶¶ 90, 91.) Defendants also allegedly attempted to conceal the use of MFNs in their agreements with the joint ventures because "they knew they would attract antitrust scrutiny by DOJ and others" (*id.* ¶ 93); one such MFN—between EMI and MusicNet—was allegedly memorialized as a "side–letter" agreement "because 'there are legal/antitrust reasons why it would be a bad idea to have MFN clauses in any, or certainly all, of these agreements'" (*id.* ¶¶ 94–95).

B. *The Second Phase: Third–Party Licensees*

According to the SCAC, Defendants also manipulated the market for Internet Music through their direct dealings with third-party licensees. (*Id.* ¶ 99.) Defendants allegedly set a "wholesale price floor at 70 cents per song [and] placed restrictions on the use

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6 The SCAC also alleges that the Recording Industry Association of America ("RIAA"), allegedly the main industry trade association and under Defendants' control, "provides another forum and means through which Defendants can communicate about the pricing, terms and use restrictions they collectively agree upon with respect to Internet Music." (SCAC ¶ 88.)

of Internet Music that unreasonably limit its utility and attractiveness to purchasers." (*Id.* ¶ 100). Agreement as to the price floor is demonstrated, argue Plaintiffs, by the fact that, in May 2005, Defendants each raised their price for Internet Music from approximately 65 cents to 70 cents. (*See* Pls.' ¶ 99 Mem. Ex. A (Proposed Third Amended Complaint).) As was the case with the joint ventures, Defendants allegedly enforced this price floor by requiring third-party licensees to sign MFNs specifying that each licensee must pay each Defendant no less than it pays other Defendants. (SCAC ¶ 99.)

The SCAC describes the experience of eMusic, allegedly the "most popular online music service that sells Internet Music owned by independent labels" (*id.* ¶ 103), which sells Internet Music for only $0.25 per song without any DRM restrictions (*id.* ¶ 103). According to the SCAC, Defendants refused to do business with eMusic, despite the fact that it is "the # 2 Internet Music retailer" (*id.* ¶ 104) because eMusic refused to impose the same Internet Music price and use restrictions as Defendants (*id.*). According to the SCAC, such uniform behavior is consistent only with prior agreement: "[a]bsent an agreement not to compete with each other, Defendants would try to gain advantages over each other by selling Internet Music with fewer unpopular restrictions; hence the lack of such competition on price or quality shows continuing collusion." (*Id.* ¶ 102.)

In addition to this conduct, the SCAC also notes that Defendants either are or were under investigation for certain conduct by various governmental agencies. For instance, Defendants' price fixing is the subject of an investigation by the Office of the New York State Attorney General (*id.* ¶ 106), and, in

2006, the DOJ "opened an investigation into collusion and price fixing of Internet Music by the Defendants" (*id.* ¶¶ 107–08). Defendants were also allegedly "subject to a number of government investigations and lawsuits concerning the pricing of CDs" (*id.* ¶ 110) and settled claims by the New York Attorney General and the FCC concerning Defendants' purported "schemes of paying radio stations for playing certain songs" (*id.* ¶ 111).

II. *DISCUSSION*

The SCAC includes three counts for relief. Count One alleges violations of § 1 of the Sherman Antitrust Act. *See* 15 U.S.C. § 1 (2000); *see also* SCAC ¶¶ 123–34. Count Two alleges violations of various state antitrust and consumer protection laws (SCAC ¶ 136(a)-(u)), and Count Three alleges unjust enrichment also under the laws of various states (*id.* ¶¶ 138–45). In their motion, Defendants argue principally that the SCAC fails to state a § 1 claim under the Supreme Court's recent decision in *Bell Atlantic v. Twombly*, 550 U.S. 544, 127 S.Ct. 1955, 1969, 167 L.Ed.2d 929 (2007); *see also* Defs.' Mem. 7. They argue that the state antitrust claims must also be dismissed for that reason (*see* Defs.' Mem. 24 n. 14) and that the consumer protection and unjust enrichment claims fail for various reasons (*see id.* at 24–28, 30–32, 34– 38). Because so much of this motion involves the pleading requirements after *Twombly*, I begin my discussion there.

A. *The Sherman Act Count*

1. Pleading Standards After *Twombly*

Rule 8(a)(2) requires "a short and plain statement of the claim showing that the pleader is entitled to relief." On a Rule 12(b)(6) motion to dismiss,

it is well-settled that a court must accept all factual allegations in the complaint as true, *Leatherman v. Tarrant County Narcotics Intelligence & Coordination Unit*, 507 U.S. 163, 164, 113 S.Ct. 1160, 122 L.Ed.2d 517 (1993), and afford the plaintiff every reasonable inference, *see Zinermon v. Burch*, 494 U.S. 113, 118, 110 S.Ct. 975, 108 L.Ed.2d 100 (1990).

It was once similarly well-settled that "a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45–46, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957). The Supreme Court retired that language in *Twombly*, however, instead holding that:

> [w]hile a complaint attacked on a Rule 12(b)(6) motion does not need detailed factual allegations, a plaintiff's obligation to provide the grounds of his entitlement to relief requires more than labels, and a formulaic recitation of the elements of a cause of action will not do. Factual allegations must be enough to raise a right to relief above the speculative level, on the assumption that all the allegations in the complaint are true (even if doubtful in fact).

*Twombly*, 127 S.Ct. at 1964–65 (internal quotation marks and citations omitted). Thus, while *Twombly* did "not require heightened fact pleading of specifics," it did require that a pleading include "enough facts to state a claim to relief that is plausible on its face." *Id.* at 1974.

To fully appreciate the significance of *Twombly*, it is necessary to understand the antitrust context in which it was decided. Because § 1 of the Sherman

Act reaches only those restraints of trade effected by "contract, combination or conspiracy," *see* 15 U.S.C. § 1; *see also Monsanto Co. v. Spray–Rite Serv. Corp.*, 465 U.S. 752, 761, 104 S.Ct. 1464, 79 L.Ed.2d 775 (1984) (§ 1 of the Sherman Act incorporates the "basic distinction between concerted and independent action"), it is fundamental that a § 1 claim allege "some form of concerted action between at least two legally distinct economic entities." *Tops Mkts., Inc. v. Quality Mkts., Inc.*, 142 F.3d 90, 95–96 (2d Cir.1998); *see also Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 775–76, 104 S.Ct. 2731, 81 L.Ed.2d 628 (1984) ("[T]his Court has recognized that § 1 is limited to concerted conduct at least since [1919]."). While such concerted action need not result from explicit agreement, *see United States v. Gen. Motors Corp.*, 384 U.S. 127, 142–43, 86 S.Ct. 1321, 16 L.Ed.2d 415 (1966), a § 1 violation based on "tacit collusion" or "conscious parallelism"[7] requires more than a bare showing of parallel conduct. *See, e.g., Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 541, 74 S.Ct. 257, 98 L.Ed. 273 (1954) ("[T]his Court has never held that proof of parallel business behavior conclusively establishes agreement or, phrased differently, that such behavior itself constitutes a Sherman Act offense. . . . '[C]onscious parallelism' has not yet read conspiracy

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[7] Those terms describe the process "by which firms in a concentrated market might in effect share monopoly power, setting their prices at a profit-maximizing, supracompetitive level by recognizing their shared economic interests and their interdependence with respect to price and output decisions." *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 227, 113 S.Ct. 2578, 125 L.Ed.2d 168 (1993).

out of the Sherman Act entirely."); *see also Twombly*, 127 S.Ct. at 1964 ("The inadequacy of showing parallel conduct or interdependence, without more, mirrors the ambiguity of the behavior: consistent with conspiracy, but just as much in line with a wide swath of rational and competitive business strategy unilaterally prompted by common perceptions of the market."). Instead, under those circumstances, "there must be evidence that tends to exclude the possibility of independent action." *Monsanto*, 465 U.S. at 768, 104 S.Ct. 1464; *see also Theatre Enters.*, 346 U.S. at 540, 74 S.Ct. 257 ("The crucial question is whether [a defendant's] conduct . . . stemmed from independent decision or from an agreement tacit or express."). Thus was born the jurisprudence of "plus factors"—the additional circumstantial evidence, beyond parallel conduct, that must exist to ensure "that the inference of conspiracy is reasonable in light of the competing inferences of independent action." *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 588, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986); *see also* ABA Section of Antitrust Law, *Antitrust Law Developments* 11 n. 57 (6th ed. 2007); 6 Philip Areeda & Herbert Hovenkamp, *Antitrust Law* §§ 1434(a)-(e) (2d ed. 2003) ("Areeda & Hovenkamp").

Whatever those "plus factors" or "factual enhancements" may be, suffice it to say for present purposes that, after *Twombly*, they must appear in a § 1 plaintiff's complaint. As the Court noted, in the antitrust context:

> [a] statement of parallel conduct, even conduct consciously undertaken, needs some setting suggesting the agreement necessary to make out a § 1 claim; without that further circumstance pointing toward a meeting of

> the minds, an account of a defendant's commercial efforts stays in neutral territory. An allegation of parallel conduct is thus much like a naked assertion of conspiracy in a § 1 complaint: it gets the complaint close to stating a claim, but without some further factual enhancement it stops short of the line between possibility and plausibility of "entitle[ment] to relief."

*Twombly*, 127 S.Ct. at 1966 (citation omitted). Rather, the Court held that "stating such a claim requires a complaint with enough factual matter (taken as true) to suggest that an agreement was made." *Id.* at 1965.

2. Assessing the SCAC After *Twombly*

At its heart, the SCAC alleges that Defendants imposed the same price and use restrictions on their sale of Internet Music to make that means of delivery of Digital Music less attractive to consumers, thereby buoying the prices of CDs.[8] Plaintiffs advance essentially three arguments to support an inference that Defendants' parallel conduct resulted from an agreement: (a) that Defendants' creation of

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[8] Plaintiffs do not argue that the joint ventures themselves violate the antitrust laws: "[I]t is not the existence or creation of these joint ventures that form the basis of the Plaintiffs' allegations. Rather, Plaintiffs allege that Defendants . . . used those ventures as a means to implement their anticompetitive agreements." Pls.' Supp. Opp'n 10; *see also Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 768, 104 S.Ct. 2731, 81 L.Ed.2d 628 (1984) (noting that joint ventures who "hold the promise of increasing a firm's efficiency and enabling it to compete more effectively" are reviewed under the rule of reason).

and participation in the joint ventures makes plausible the inference that their subsequent parallel conduct was the result of an agreement; (b) that further factors—acts against Defendants' economic self-interests, motive to conspire, suspicious price increases, Defendants' "antitrust record" and opportunities to conspire through the RIAA (see Pls.' Opp'n 9–12)—indicate that Defendants' parallel conduct resulted from agreement; and (c) that certain economic indicators—market concentration and high barriers to market entry—are sufficient to ground a § 1 conspiracy (*see id.* at 8–9, 11). I discuss each individually below and, affording Plaintiffs every reasonable inference, *see Zinermon*, 494 U.S. at 118, 110 S.Ct. 975, conclude that the further facts alleged by Plaintiffs, considered alone and collectively, do not place Defendants' conduct "in a context that raises a suggestion of a preceding agreement." *Twombly*, 127 S.Ct. at 1966. Therefore, Plaintiffs fail to state a claim for relief under § 1 of the Sherman Act and Count 1 of the SCAC must be DISMISSED.

a. The Joint Ventures

Because Plaintiffs do not challenge the legality of the joint ventures themselves, it is somewhat unclear how they contend those ventures support an inference of agreement. They appear to argue that the creation and operation of the joint ventures yields an inference of agreement because those ventures were mere sham organizations designed solely to provide a forum in which to discuss and agree to the terms of the later agreement.

To begin, the bald allegation that the joint ventures were shams is conclusory and implausible. It ignores the context in which those entities were created: an environment of widespread unauthorized

downloading of Internet Music. (*See, e.g.*, Almeida Decl. Ex. B (*Bulcao* Compl.) ¶ 37 ("The distribution of digital music exploded in the late 1990s with the emergence of Napster, the most popular online music service (which had tens of millions of users) Kazaa and other services offering free peer to peer file sharing, *i.e.*, the ability of one person to share Online Music with anyone else via a website. . . . Napster initially provided file sharing for free. . . .").)[9] As a result of that unauthorized downloading, "the major recording companies that control the copyrights to most popular music [were] generally unwilling to license their music for online sale except in protected formats." (*See id.* Ex. C (*Tucker* Compl.) ¶¶ 33–34.)[10] Viewed in that context, each reason offered by Plaintiffs to support their sham allegation has an entirely reasonable independent justification: "unpopular" use restrictions and compromise in the collaboration's pricing structure are each consistent with a collaborative effort to address widespread music piracy. In the absence of any formal veil-piercing allegations and without challenging the legality of those joint ventures under the antitrust laws, Plaintiffs cannot now call into question their legitimacy simply

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[9] I may consider the Bulcao complaint as a predecessor to the SCAC. *See United States v. GAF Corp.*, 928 F.2d 1253, 1259 (2d Cir. 1991) ("[T]he law is quite clear that superseded pleadings in civil cases may constitute admissions of party opponents, admissible in the case in which they were originally filed, as well as any subsequent litigation involving that party." (citing *United States v. McKeon*, 738 F.2d 26, 31 (2d Cir. 1984))).

[10] I am permitted to take judicial notice of the Tucker complaint under Rule 201(b) of the Federal Rules of Evidence. *See Kramer v. Time Warner Inc.*, 937 F.2d 767, 773 (2d Cir.1991).

by describing conduct consistent with rational business decisions. For that reason alone, I could decline to infer that the joint ventures were vehicles to create an antitrust conspiracy.

There is a further reason, however, not to draw such a negative inference. It is common sense that some level of information sharing must inevitably occur in the operation of a joint venture. As Judge Marilyn Hall Patel recently observed in a passage upon which Plaintiffs rely, "even a naïf must realize that in forming and operating a joint venture, [record label] representatives must necessarily meet and discuss pricing and licensing." *In re Napster, Inc. Copyright Litig.*, 191 F.Supp.2d 1087, 1109 (N.D. Cal. 2002). Judge Patel drew a negative inference from the possibility of such communication, allowing further discovery into Napster's allegation that the joint ventures themselves violated the antitrust laws. *See id.* at 1108–10. Of course, Plaintiffs offer no direct challenge to the joint ventures here. This situation is, therefore, more like the situation in *Twombly*, where the Supreme Court declined to draw a negative inference from allegations of information sharing that resulted from defendants' participation in a concededly legal industry trade group. *See* 127 S.Ct. at 1971 n. 12. It is similarly unwarranted to draw a negative inference from allegations involving the unchallenged collaboration between and among Defendants.[11]

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[11] Plaintiffs' allegation that Defendants "conspired to mask their anticompetitive conduct by pretextually establishing rules to prevent antitrust violations" (SCAC ¶ 90) is wholly conclusory. Further, I decline to infer that the joint ventures were designed to hide a true purpose of information sharing simply

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A more subtle argument could be made that a later illegal tacit agreement can be inferred from the fact of Defendants' explicit prior agreement with materially the same terms, reached in the context of the joint ventures. What scarce authority there is on this issue—the parties have cited no reported decision, and research has disclosed but one—does not address the precise issue. *See United States v. Nat'l Malleable & Steel Castings Co.*, Civ. No. 30,281, 1957 U.S. Dist. Lexis 4209, 1957 Trade Cas. ¶ 68,890 (N.D. Oh. Nov. 26, 1957), *affirmed*, 358 U.S. 38, 79 S.Ct. 39, 3 L.Ed.2d 44 (1958) (mem.). In the *Steel Castings* case, the court confronted a price-fixing conspiracy that was alleged to have existed after defendants discontinued a trust agreement among themselves. *See id.* at *10–12. Though its legality was unchallenged, all appear to have agreed that the prior trust agreement was discontinued because it would have been considered illegal under then-recent changes in the law. *See id.* at *12. The court refused to conclude that the prior trust agreement was illegal; the court further refused to conclude that the prior agreement had "ended only in its outward manifestations" based on certain economic evidence and other testimony about the market in question. *See id.* at *19–20.[12]

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because Defendants structured them so as to comply with the antitrust laws.

12 Some guidance may also be taken from the cases limiting the inference that may be drawn from allegations of antitrust conspiracy in other markets, *see, e.g.*, *Matsushita*, 475 U.S. at 595–96, 106 S.Ct. 1348, or from commentary recognizing the

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I conclude that an inference of subsequent agreement based on prior, unchallenged explicit agreement is unreasonable. By not challenging the legality of the joint ventures, Plaintiffs concede the possibility that Defendants, acting collectively through the joint ventures, were permissibly motivated in imposing the price and use restrictions in question. *Cf.* U.S. Dep't of Just. & Fed. Trade Comm'n, *Antitrust Guidelines for Collaborations Among Competitors* 5–6 (2000) (recognizing that joint ventures offer significant pro-competitive benefits) Conceding that possibility, it is just as likely that each Defendant was motivated on its own by the same permissible impulses that motivated the group as a collective, and Plaintiffs offer nothing now to create a reasonable inference that Defendants were not so motivated.[13]

For these reasons, I reject as unreasonable Plaintiffs' invitation to infer that Defendants' subsequent adoption of parallel price and use restrictions re-

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limits of allegations of earlier conspiracy in the same market, *see* 6 Areeda & Hovenkamp, *supra*, § 1421b(3). Of course, the inference of agreement is weaker here *a fortiori* because Plaintiffs do not claim that the joint ventures were illegal.

[13] Inertia is yet another possible explanation for Defendants' parallel conduct that does not implicate prior agreement. As Areeda and Hovenkamp discuss, parallel conduct can just as easily result from convention, under which circumstances an inference of prior agreement is illogical. *See* 6 Areeda & Hovenkamp, *supra*, § 1410c (quoting and discussing D. Lewis, Convention: *A Philosophical Study* (1969)).

sulted from agreement based on their creation of or membership in the unchallenged joint ventures.

b. Other Circumstantial Evidence

The other circumstances alleged by Plaintiffs are similarly equivocal and do not justify the inference that Defendants' parallel conduct resulted from agreement. For instance, Plaintiffs' allegation of a "motive to conspire" is nothing more than an assertion of interdependence. Plaintiffs contend that Defendants possessed such a motive because they understood that price competition among them would only drive down the price of Digital Music. (See SCAC ¶ 83.) There is no agreement, however, merely because an oligopolist charges an inflated price knowing (or even hoping) that other oligopolists will match his high price. Such is bald conscious parallelism, and, as the Supreme Court has stated, "parallel conduct, even conduct consciously undertaken," does not itself state an antitrust conspiracy. *See Twombly*, 127 S.Ct. at 1966; *see also* 6 Areeda & Hovenkamp, *supra*, § 1433 (surveying cases); *id.* § 1432a (concluding that no agreement exists "*merely* from recognized interdependence without the addition of any facilitators").

As noted above, the Supreme Court observed in *Twombly* that the mere participation in an industry trade association would not yield an inference of improper inter-firm communication. *See* 127 S.Ct. at 1971 n. 12. Plaintiffs' allegation concerning the RIAA in this action suffers a similar fate. That fact is, at best, neutral and thus adds nothing that would "'nudge [plaintiffs'] claims across the line from conceivable to plausible.'" *In re Elevator Antitrust Litig.*, 502 F.3d 47, 50 (2d Cir. 2007) (quoting *Twombly*, 127 S.Ct. at 1974).

Plaintiffs' allegation that Defendants' "antitrust record" supports an inference of agreement is even less helpful. First, Plaintiffs overstate the weight that should be afforded to such evidence. *See* 6 Areeda & Hovenkamp, *supra*, § 1421b(1) ("prior conspiracy is not alone probative of present collusion"); Richard A. Posner, *Antitrust Law* 79 (2d ed. 2001) (antitrust record of an industry is useful to help enforcement agencies target limited resources). Indeed, as one commentator has suggested, "caution is required lest the defendants' demonstrated moral infirmities distract the court's attention from the distinction between tacit coordination through mere interdependence and traditional conspiracy." 6 Areeda & Hovenkamp, *supra*, § 1421b(2). Still greater caution is required here, where the alleged "antitrust record" hardly illustrates any "demonstrated moral infirmities." As at least one other court has noted, mere investigation by governmental agencies does not show an "antitrust record." *See In re Graphics Processing Units Antitrust Litig.*, 527 F.Supp.2d 1011, 1024 (N.D. Cal. 2007) (investigation alone "carries no weight in pleading an antitrust conspiracy claim"). Moreover, the investigations alleged here do not support the inference Plaintiffs urge: the DOJ closed its investigation after it "uncovered no evidence that the major record labels' joint ventures have harmed competition or consumers of digital music" (Almeida Decl. Ex. 5 (DOJ Press Release)), and the relevance of the New York State Attorney General's payola investigation is not apparent. Such an "antitrust record" cannot justify the already problematic inference that "once a criminal, always a criminal."

Plaintiffs' conclusion that the imposition of price and use restrictions was against Defendants' eco-

nomic self-interests is implausible and, likewise, cannot support an inference of agreement. As discussed above, the imposition of use restrictions was, in fact, not contrary to Defendants' collective economic self-interests when viewed against the backdrop of widespread unauthorized music downloading. (*See supra* 442.) That observation remains true for each individual Defendant. Indeed, contrary to Plaintiffs' suggestion, the unpopularity of Defendants' Internet Music use restrictions with consumers is hardly reflective of each Defendant's economic self-interest. (*See* SCAC ¶ 76 ("Any one of the Defendants right have removed these unpopular DRM and gained additional market share and profits . . . .").) Surely, any Defendant who decided to give its product away for free would have been popular with consumers, but refusing to do so is hardly the economically-irrational decision Plaintiffs portray it to be. Especially under the circumstances of widespread pirating, the fact that customers disliked each Defendant's attempt to secure its copyrights shows nothing. Nor do Plaintiffs derive support from the fact that the price for Defendants' Internet Music converged at a higher price than that charged by the independent music labels. It is beyond peradventure that different products will fetch different prices, and, though the parties have not briefed the issue of what price disparity would be reasonable here. I need not decide that issue to conclude that the mere existence of a disparity does not itself bespeak an act against self-interest.

Finally, Plaintiffs' ambiguous allegation of price increases does not support an inference of agreement

because that conduct, as alleged, is consistent with sequential parallelism.[14] As commentators note, "[n]o additional fact, such as advance agreement, is needed to explain that process," and, therefore, "agreement is ordinarily more difficult to infer from sequential actions." 6 Areeda & Hovenkamp, *supra*, § 1425d(1). On the other hand, an inference of prior agreement may be warranted from simultaneous parallel price conduct where no actor had prior knowledge of or time to consider the other actors' conduct. *See Taxi Weekly, Inc. v. Metro. Taxicab Board of Trade, Inc.*, 539 F.2d 907, 911–12 (2d Cir. 1976) (inference of prior agreement justified where taxi fleet owners each called to cancel subscription to trade publication within one half hour of each other one day after meeting); *see also* 6 Areeda & Hovenkamp, *supra*, § 1425c. Here, Plaintiffs allege only that prices rose "in or about May 2005." Affording Plaintiffs every reasonable inference, *Twombly* nevertheless requires that they plead further facts tending to show conspiracy; "facts" such as these that are just as consistent with independent action are insufficient as a matter of law. *See, e.g.*, *Matsushita*, 475 U.S. at 588, 106 S.Ct. 1348 ("[C]onduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy . . . ." (citing *Monsanto*, 465 U.S. at 764, 104 S.Ct. 1464)).

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[14] Plaintiffs seek leave to amend SCAC Paragraph 99. Because I conclude that their proposed amendment would be futile, leave to amend is DENIED. *See Foman v. Davis*, 371 U.S. 178, 182, 83 S.Ct. 227, 9 L.Ed.2d 222 (1962); *Jin v. Metro. Life Ins. Co.*, 310 F.3d 84, 101 (2d Cir. 2002).

c. Economic Indicators

Finally, Plaintiffs suggest that the existence of certain economic indicators is sufficient to justify the inference that Defendants' parallel conduct resulted from agreement. (*See* Pls.' Opp'n 9.) For this proposition, they rely principally on the work of Judge Richard A. Posner, who describes an approach to identifying and punishing tacit antitrust collusion based solely on economic evidence. *See* Posner, *supra*, at 69. That approach posits two sets of economic data: indicators that "identif[y] those markets in which conditions are propitious for the emergence of collusion" and indicators that reveal "whether there really is collusive pricing in any of those markets." *Id.* The first set of indicators, while valuable to help enforcement agencies direct limited resources, *see id.* at 69, 79, do not show that the alleged conduct "stemmed from independent decision or from an agreement, tacit or express." *Theatre Enters.*, 346 U.S. at 540, 74 S.Ct. 257.

Without reaching the question whether economic evidence alone may be sufficient to support an inference of agreement,[15] Plaintiffs' attempt to do so here

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15 Judge Posner observes how judicial treatment of the "plus factors" analysis has often mistakenly demanded evidence of actual agreement: "[w]hat the cases seem to *mean*, however, and what some of them make explicit, is that there must be an explicit agreement based upon actual communication between the parties." *See* Posner, *supra*, at 94 (emphasis in original, footnote omitted); *see id.* at 99–100 (discussing language in Monsanto that aggravates judicial confusion regarding proof of tacit agreement). He argues against that requirement: "[i]f the economic evidence presented in a case warrants an inference of collusive pricing, there is neither legal nor practical justifica-

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fails on its own terms. In this case, Plaintiffs allege only facts that would identify the market for Digital Music as one "in which conditions are propitious for the emergence of collusion."[16] (See SCAC ¶¶ 6 (high seller-side concentration), 47 (low buyer-side concentration), 70–71 (similar cost structures among Defendants), 72 (industry-wide cooperative practices).)[17] As Judge Posner recognizes, however,

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tion for requiring evidence that will support the further inference that the collusion was explicit rather than tacit." *See id.* at 94.

[16] Plaintiffs allege that the Digital Music market is characterized by low buyer-side concentration because "there are thousands of class members." (*See* Pls.' Opp'n 9.) That assertion is undermined somewhat by the allegation elsewhere in the SCAC that Defendants sold largely to retailers (*see* SCAC ¶¶ 56–57, 79), a group as to whose size the SCAC is silent. Further, it is worth noting that SCAC's description of the market for Internet Music is inconsistent in some basic respects with the type of market Judge Posner describes as vulnerable to price collusion. That is to say, as it is described in the SCAC, the Internet Music market is not characterized by the relative inability of competitors to increase supply or decrease prices to challenge effectively the conspirators' market control, *see* Posner, *supra*, at 63–64, but rather as one where, for instance, eMusic was able to increase its "production" rapidly through relationships with "hundreds of independent record labels," sufficient even to surpass Defendants in the market (*see* SCAC ¶ 104).

[17] It should be noted that the paragraphs in the SCAC invoked to support the claim that Plaintiffs have pleaded high barriers to market entry (see Pls.' Opp'n 11 (citing SCAC ¶¶ 55–57)) do not mention barriers to market entry. Paragraph 55 states: "Defendants have acted on grounds generally applicable to the entire Class, thereby making final injunctive relief

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those facts do not render plausible the inference of agreement among these Defendants: just because you grow up in a high crime area does not make you a criminal.

For the foregoing reasons, I conclude that the SCAC does not allege the further facts required by *Twombly* to state a § 1 claim based upon parallel conduct. Count One is, therefore, DISMISSED.

B. *The State Antitrust and Consumer Protection Count*

1. The State Antitrust Claims

As noted above, Count Two of the SCAC asserts claims under the antitrust laws of the following 16 jurisdictions: Arizona, California, Washington, D.C., Iowa, Kansas, Maine, Michigan, Minnesota, Nevada, North Carolina, North Dakota, South Dakota, Tennessee, Vermont, West Virginia and Wisconsin.[18]

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or corresponding declaratory relief appropriate with respect to the Class as a whole." Paragraphs 56 and 57 duplicate each other, and state: "Defendants produce, license and distribute Digital Music, including Internet Music and CDs, to retailers for sale throughout the United States and in some instances sell Internet Music and CDs directly to consumers through Internet sites, record clubs and other entities which they own or control."

[18] Paragraph 136(n) of the SCAC purports to assert claims under the "New York common law against restraints of trade." New York law includes an antitrust provision, called the Donnelly Act. *See* N.Y. Gen. Bus. Law § 340 *et seq.* (McKinney 2004). Nevertheless, Plaintiffs state that it is not their intention to bring any claim under that Act (*see* Pls.' Opp'n 29 n.29); and they do not discuss or even identify the distinct "common

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Defendants argue that those claims must be dismissed for the same reason as the federal claim. I agree.

At its heart, *Twombly* is a decision about the Federal Rules of Civil Procedure: to survive a Rule 12(b)(6) motion to dismiss, a pleading must include allegations that make its claim for relief plausible, not merely possible. *See* 127 S.Ct. at 1974 (pleading must include "enough facts to state a claim to relief that is plausible on its face"). That purely procedural standard of pleading binds this Court's evaluation of state law claims, *see, e.g.*, 5B Charles Alan Wright & Arthur R. Miller, *Federal Practice & Procedure* § 1357 (3d ed. 2008), and, while it has caused much ado in the legal community, *see, e.g., Iqbal v. Hasty*, 490 F.3d 143, 155 (2d Cir. 2007) (finding "[c]onsiderable uncertainty concerning the standard for assessing the adequacy of pleadings" after *Twombly* ), it did not alter the substantive federal law of antitrust: parallel conduct alone, even if consciously undertaken by individual firms, does not

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law against restraints of trade" upon which to base their claim. Therefore, to the extent the SCAC asserts claims under New York law apart from its claims under New York's Consumer Protection from Deceptive Acts and Practices provisions, *see* N.Y. Gen. Bus. Law § 346 (McKinney 2004), those claims are DISMISSED. In any event, the substantive provisions of the Donnelly Act mirror federal antitrust law, *see, e.g., State v. Mobil Oil Corp.*, 38 N.Y.2d 460, 463, 381 N.Y.S.2d 426, 344 N.E.2d 357, 359 (1976); *Reading Int'l, Inc. v. Oaktree Capital Mgmt. LLC*, 317 F.Supp.2d 301, 333 (S.D.N.Y. 2003), and, thus, any New York antitrust claims would be dismissed for the same reasons as were the federal and other state antitrust claims.

constitute a conspiracy to restrain trade in violation of § 1 of the Sherman Act. The question, therefore, is not whether the relevant state courts would decide *Twombly* the same way but, rather, whether the state's antitrust law incorporates the same substantive principle of federal antitrust law regarding conscious parallelism.

I answer this question in the affirmative for several reasons. First, some courts have explicitly adopted, as a matter of state substantive antitrust law, the federal approach to the question of whether consciously parallel conduct alone constitutes an antitrust conspiracy.[19] Second, several states' anti-

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[19] *See Aguilar v. Atl. Richfield Co.*, 25 Cal.4th 826, 851–52, 107 Cal.Rptr.2d 841, 24 P.3d 493, 511–12 (2001) ("Ambiguous evidence or inferences showing or implying conduct that is as consistent with permissible competition by independent actors as with unlawful conspiracy by colluding ones do not allow such a trier of fact [to find an unlawful conspiracy]." (citing Areeda & Hovenkamp)); *Pease v. Jasper Wyman & Son*, 00 Civ. 15, 2002 WL 1974081, at *11–12 (Me. Super. Ct. Aug. 9, 2002); *Desgranges Psychiatric Ctr., PC v. Blue Cross & Blue Shield of Mich.*, 124 Mich.App. 237, 244–45, 333 N.W.2d 562, 565 (Mich. Ct. App. 1983) ("A unilateral action, no matter how anticompetitive it may be, does not amount to a combination to restrain trade.") (citing *Theatre Enters.*, 346 U.S. at 537, 74 S.Ct. 257); *Wrensch v. Assoc. Milk Producers, Inc.*, No. 78–131, 1979 WL 30778, at *6 n. 21 (Wis. Ct. App.1979) ("We recognize that similar practices by competitors, *i.e.*, 'conscious parallelism,' will sometimes support an inference of an agreement. Only where the pattern of action undertaken is inconsistent with the self-interest of the individual actors, were they acting alone, may an agreement be inferred solely from such parallel action." (quotation marks omitted)); *State v. Heritage Realty of Vermont*, 137 Vt. 425, 429–30, 407 A.2d 509, 511–12 (1979) ("Price uniformity among competitors does not, of itself, violate the antitrust laws,

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trust statutes explicitly direct state courts to consider, as persuasive or controlling authority, federal court decisions construing the federal antitrust laws.[20] Third, even absent such a statutory mandate, the courts in each jurisdiction overwhelmingly look to federal antitrust decisions to construe their

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however. If it is the result of independently reached pricing decisions, the element of 'agreement' necessary to establish an illegal price-fixing combination or conspiracy is absent." (citations omitted)).

[20] *See* Ariz. Rev. Stat. § 44–1412 (2008) ("It is the intent of the legislature that in construing this article, the courts may use as a guide interpretations given by the federal courts to comparable federal antitrust statutes."); D.C. Code § 28–4515 (2008) ("It is the intent of the Council of the District of Columbia that in construing this chapter, a court of competent jurisdiction may use as a guide interpretations given by federal courts to comparable antitrust statutes."); Iowa Code § 553.2 (2008) ("This chapter shall be construed to complement and be harmonized with the applied laws of the United States which have the same or similar purpose as this chapter."); Mich. Comp. Laws 445.784(2) (2008) ("It is the intent of the legislature that in construing all sections of this act, the courts shall give due deference to interpretations given by the federal courts to comparable antitrust statutes. . . ."); Nev. Rev. Stat. § 598A.050 (2008) ("The provisions of this chapter shall be construed in harmony with prevailing judicial interpretations of the federal antitrust statutes."); S.D. Codified Laws § 37–1–22 (2008) ("It is the intent of the Legislature that in construing this chapter, the courts may use as a guide interpretations given by the federal or state courts to comparable antitrust statutes."); W. Va. Code § 47–18–16 (2008) ("This article shall be construed liberally and in harmony with ruling judicial interpretations of comparable federal antitrust statutes.").

own antitrust statutes.[21] It is irrelevant that states have declined to follow federal antitrust law for the

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[21] The following authorities are organized by jurisdiction. Arizona: *See Johnson v. Pac. Lighting Land Co.*, 817 F.2d 601, 604 (9th Cir. 1987) (noting that "United States Supreme Court Sherman Act decisions [are] used to construe Arizona antitrust statute") citing *Three Phoenix Co. v. Pace Indus., Inc.*, 135 Ariz. 113, 659 P.2d 1258, 1260 (1983); *see also Brooks Fiber Commc'ns of Tucson, Inc. v. GST Tucson Lightwave, Inc.*, 992 F.Supp. 1124, 1130 (D.Ariz.1997). California: *See Corwin v. Los Angeles Newspaper Serv. Bureau, Inc.*, 4 Cal.3d 842, 852, 94 Cal. Rptr. 785, 484 P.2d 953, 959 (1971) ("Sections 16720 and 16726 of the Cartwright Act were patterned after the Sherman Act and decisions under the latter act are applicable to the former."); *see also County of Tuolumne v. Sonora Cmty. Hosp.*, 236 F.3d 1148, 1160 (9th Cir. 2001) (dismissing state antitrust claims because "[t]he analysis under California's antitrust law mirrors the analysis under federal law because [it] was modeled after the Sherman Act" (citing *Mailand v. Burckle*, 20 Cal.3d 367, 375, 143 Cal.Rptr. 1, 572 P.2d 1142, 1147 (1978))). District of Columbia: *See WAKA LLC v. DC Kickball*, 517 F.Supp.2d 245, 252 (D.D.C.2007) (failure to state a claim under § 1 equated to failure to state a claim under D.C. antitrust provision); *GTE New Media Servs., Inc. v. Ameritech Corp.*, 21 F.Supp.2d 27, 45 (D.D.C. 1998) ("The only difference between the two statutes is that the D.C. Code does not require an interstate nexus, but rather a connection within this jurisdiction."); *Mazanderan v. In-dep. Taxi Owners' Assoc., Inc.*, 700 F.Supp. 588, 591 n. 9 (D.D.C. 1988) ("Analysis of plaintiff's state antitrust claim necessarily follows that of the federal claim. . . . "). Iowa: *See Davies v. Genesis Med. Ctr. Anesthesia & Analgesia, P.C.*, 994 F.Supp. 1078, 1103 (S.D. Iowa 1998) ("When interpreting Iowa antitrust statutes, Iowa courts are required by section 553.2 to give considerable weight to federal cases construing similar sections of the Sherman Act."); *see also Fed. Land Bank of Omaha v. Tiffany*, 529 N.W.2d 294, 296–97 (Iowa 1995) (federal decisions about whether farm credit banks are subject to federal antitrust laws was dispositive of same ques-

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tion under Iowa antitrust law). Kansas: *See Orr v. Beamon*, 77 F.Supp.2d 1208, 1211–12 (D. Kan. 1999) ("While recognizing that federal antitrust cases are not binding on the court in interpreting Kansas antitrust statutes, the court finds such cases sufficiently persuasive to guide its decision. . . ."); *Bergstrom v. Noah*, 266 Kan. 829, 845, 974 P.2d 520, 531 (1999) ("While such cases may be persuasive authority for any state court interpreting its antitrust laws, such authority is not binding upon any court in Kansas interpreting Kansas antitrust laws."). Maine: *See Davric Maine Corp. v. Rancourt*, 216 F.3d 143, 149 (1st Cir. 2000) ("We have noted that the 'Maine antitrust statutes parallel the Sherman Act,' and thus have analyzed claims thereunder according to the doctrines developed in relation to federal law." (quoting *Tri–State Rubbish, Inc. v. Waste Mgmt., Inc.*, 998 F.2d 1073, 1081 (1st Cir. 1993))). Michigan: *See First Med Representatives, LLC v. Futura Med. Corp.*, 195 F. Supp. 2d 917, 922 (E.D. Mich. 2002) ("[B]ecause Michigan courts apply Sherman Act analysis to the MARA, the following analysis applies to the entirety of Count I, for the allegations of both state and federal antitrust violations." (citing *Blair v. Checker Cab Co.*, 219 Mich.App. 667, 675, 558 N.W.2d 439 (Mich. Ct. App.1996))); *Danou v. Kroger Co.*, 557 F.Supp. 1266, 1268 (E.D. Mich.1983) ("The Michigan antitrust statute is patterned after the Sherman Act. Accordingly, the federal courts' interpretations of the Sherman Act are persuasive authority as to the meaning of the Michigan Act.") (citing *Goldman v. Loubella Extendables*, 91 Mich.App. 212, 283 N.W.2d 695 (Mich. Ct. App.1979)). Minnesota: *See State by Humphrey v. Alpine Air Prods., Inc.*, 490 N.W.2d 888, 894 (Minn.Ct.App.1992) ("Minnesota antitrust law should be interpreted consistently with federal court interpretations of the Sherman Act unless state law is clearly in conflict with federal law."); *see also Lamminen v. City of Cloquet*, 987 F.Supp. 723, 734 (D. Minn.1997) (same). North Carolina: *See Rose v. Vulcan Materials Co.*, 282 N.C. 643, 655, 194 S.E.2d 521, 530 (1973) ("[T]he body of law applying the Sherman Act, although not binding upon this Court in applying [North Carolina's antitrust law], is nonetheless instructive in

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determining the full reach of that statute."); *see also United Roasters, Inc. v. Colgate-Palmolive Co.*, 485 F.Supp. 1041, 1047–48 (E.D.N.C. 1979) ("[C]aution must be exercised in [taking guidance from Sherman Act decisions] because the Sherman Act is in some respects broader than [North Carolina's antitrust law]."). *South Dakota: See Byre v. City of Chamberlain*, 362 N.W.2d 69, 74 (S.D. 1985) ("[B]ecause of the legislative suggestion for interpretation found in SDCL 37–1–22, great weight should be given to the federal cases interpreting the federal statute."); *see also In re S.D. Microsoft Antitrust Litig.*, 707 N.W.2d 85, 100 (S.D.2005) (reiterating *Byre*); *Assam Drug Co., Inc. v. Miller Brewing Co., Inc.*, 624 F.Supp. 411, 412 (D.S.D. 1985) ("[F]ederal court interpretations of the federal antitrust statutes may be used as a guide in interpreting the South Dakota statutes cited by plaintiffs in this case [and, therefore,] it is appropriate for correct analysis of the issues presented by this motion to refer to the relevant federal law."). Vermont: *See State v. Heritage Realty of Vermont*, 137 Vt. 425, 429– 30, 407 A.2d 509, 511–12 (1979) (analyzing claim under Vermont antitrust law exclusively by reference to federal court Sherman Act decisions). West Virginia: *See Kessel v. Monongalia County Gen. Hosp. Co.*, 220 W.Va. 602, 610, 648 S.E.2d 366, 374 (2007) ("[T]he Legislature has directed that the [West Virginia antitrust law] 'shall be construed liberally and in harmony with ruling judicial interpretations of comparable federal antitrust statutes.'" Moreover, this Court held . . . that "[t]he courts of this state are directed by the legislature . . . to apply the federal decisional law interpreting the Sherman Act . . . to our own parallel antitrust statute." (citations omitted)). *Wisconsin: See State v. Waste Mgmt. of Wis., Inc.*, 81 Wis.2d 555, 574, 261 N.W.2d 147, 155 (1978) ("Except for the fact that the state act applies to intrastate commerce while the federal act applies to interstate commerce, what amounts to a conspiracy in restraint of trade under the Sherman Act amounts to a conspiracy in restraint of trade under the Wisconsin antitrust act."); *see also Indep. Milk Producers Co-op v. Stoffel*, 102 Wis.2d 1, 6, 298 N.W.2d 102, 104 (Wis.Ct.App.1980) ("[The Wisconsin Antitrust

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proposition that indirect purchasers lack standing to sue. *See Illinois Brick Co. v. Illinois*, 431 U.S. 720, 97 S.Ct. 2061, 52 L.Ed.2d 707 (1977). As the Supreme Court of Iowa explained:

> The purpose behind both state and federal antitrust law is to apply a uniform standard of conduct so that businesses will know what is acceptable conduct and what is not acceptable conduct. To achieve this uniformity or predictability, we are not required to define who may sue in our state courts in the same way federal courts have defined who may maintain an action in federal court.
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> . . .
>
> Harmonizing our construction and interpretation of state law as to what conduct is governed by the law satisfies the harmonization provision.

*Comes v. Microsoft Corp.*, 646 N.W.2d 440, 446 (Iowa 2002); *accord Hyde v. Abbott Labs., Inc.*, 123 N.C.App. 572, 579, 473 S.E.2d 680, 685 (N.C. Ct. App.1996) (declining to follow *Illinois Brick* for other reasons). That is to say, disagreement about who can sue does not entail disagreement about when they may recover. Finally, however, the simple fact remains that each state statute requires some form

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law] is drawn largely from federal antitrust law. Interpretation of [the Wisconsin law], prohibiting conspiracies in restraint of trade or commerce, is controlled by federal case law." (citing *Grams v. Boss*, 97 Wis.2d 332, 346, 294 N.W.2d 473, 480 (1980))).

of agreement,[22] and independently undertaken parallel conduct, even if undertaken consciously, does

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[22] *See* Ariz. Rev. Stat. § 44–1402 (prohibiting "[a] contract, combination or conspiracy between two or more persons in restraint of, or to monopolize, trade or commerce"); Cal. Bus. & Prof. Code § 16720 (2008) ("A trust is a combination of capital, skill or acts by two or more persons for any of the following purposes."); D.C. Code § 28–4502 (prohibiting "[e]very contract, combination in the form of a trust or otherwise, or conspiracy in restraint of trade or commerce."); Iowa Code § 553.4 ("A contract, combination, or conspiracy between two or more persons shall not restrain or monopolize trade or commerce"); Kansas Stat. Ann. § 50–101 (2008) (defining "[a] trust is a combination of capital, skill, or acts, by two or more persons"); Me. Rev. Stat. Ann. tit. 10, § 1101 (2008) (prohibiting "[e]very contract, combination in the form of trusts or otherwise, or conspiracy, in restraint of trade"); Mich. Comp. Laws § 445.772 (prohibiting "[a] contract, combination, or conspiracy between 2 or more persons in restraint of, or to monopolize, trade or commerce"); Minn. Stat. § 325D.51 (2008) (prohibiting "[a] contract, combination, or conspiracy between two or more persons in unreasonable restraint of trade or commerce"); Nev. Rev. Stat. § 598A.060 (enumerating and prohibiting various types of agreements that "constitute[ ] a contract, combination or conspiracy in restraint of trade"); N.C. Gen. Stat. § 75–1 (2008) (prohibiting "[e]very contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade"); N.D. Cent. Code § 51–08.1–02 (2008) (prohibiting "[a] contract, combination, or conspiracy between two or more persons in restraint of, or to monopolize, trade or commerce"); S.D. Codified Laws § 37–1–3.1 (prohibiting "[a] contract, combination, or conspiracy between two or more persons in restraint of trade or commerce"); Tenn. Code Ann. § 47–25–101 (2008) (prohibiting "[a]ll arrangements, contracts, agreements, trusts, or combinations between persons or corporations made with a view to lessen, or which tend to lessen, full and free competition"); W. Va. Code § 47–18–3 (prohibiting "[e]very contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce");

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not itself demonstrate agreement. For those reasons and in light of my discussion of the federal claims, the state antitrust claims are DISMISSED.

2. State Consumer Protection Claims

As noted above, Count Two of the SCAC also asserts claims under the consumer protection laws of the following eight jurisdictions: California, Washington D.C., Florida, Maine, Massachusetts, Nebraska, New Mexico and North Carolina.[23] To support those claims, Plaintiffs allege the same conduct that forms the basis of their antitrust claims. (*See, e.g.*, Pls.' Opp'n 2 ("The pertinent state consumer protection laws encompass price-fixing claims because price fixing is a form of unfair, unconscionable or deceptive conduct."); *see also id.* at 34 n.39.) While the statutes at issue may embrace a violation of federal antitrust laws as a grounds for relief,[24] my con-

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Wis. Stat. § 133.03 (2008) (prohibiting "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce").

23 While the SCAC asserts claims broadly under the Kansas Unfair Trade and Consumer Protection Act, *see* Kansas Stat. Ann. ch. 50 *see also SCAC* ¶ 136(f), Plaintiffs clarify that they assert only claims under Article 1 of that Act, prohibiting certain restraints of trade, *see id.* § 50–101 *et seq.*, and not the portion of Article 6 of that Act entitled the Kansas Consumer Protection Act, *see id.* § 50–623 *et seq.*; *see also* Pls.' Opp'n 33.

24 *See, e.g.*, Fla. Stat. § 501.203(3)(c) (2008) (Florida's consumer protection act violated by violations of "[a]ny law, statute, rule, regulation, or ordinance which proscribes unfair methods of competition, or unfair, deceptive, or unconscionable acts or practices"); 940 Mass. Code Regs. 3.16(4) (2008) (Massa-

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clusion that Plaintiffs have not adequately alleged such a violation necessarily precludes their attempt to recast that violation as an unfair business practice.[25]

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chusetts consumer protection act violated by violation of the "the Federal Trade Commission Act, the Federal Consumer Credit Protection Act or other Federal consumer protection statutes"); *see also Sunbelt Television, Inc. v. Jones Intercable, Inc.*, 795 F.Supp. 333, 338 (C.D. Cal. 1992) ("Here since plaintiffs have adequately plead a violation of the Sherman Act, they have clearly stated a cause of action under California's Unfair Competition law."); *Dist. Cablevision Ltd. P'ship v. Bassin*, 828 A.2d 714, 723 (D.C. 2003) ("Trade practices that violate other laws, including the common law, also fall within the purview of the [Washington D.C. Consumer Protection Procedures Act]."); *Mack v. Bristol-Myers Squibb Co.*, 673 So.2d 100, 104 (Fla. Ct. App. 1 Dist.1996) ("Thus, the acts proscribed by subsection 501.204(1) include antitrust violations."); *Triple 7, Inc. v. Intervet, Inc.*, 338 F.Supp.2d 1082, 1087 (D. Neb. 2004) (Nebraska consumer protection statute violated by violations of Sherman Act); *ITCO Corp. v. Michelin Tire Corp.*, 722 F.2d 42, 48 (4th Cir. 1983) ("We thus hold that proof of conduct violative of the Sherman Act is proof sufficient to establish a violation of the North Carolina Unfair Trade Practices Act.").

[25] *See, e.g., In re Tamoxifen Citrate Antitrust Litig.*, 466 F.3d 187, 198 (2d Cir. 2006) (affirming district court's dismissal of state consumer protection claims upon district court's conclusion that plaintiffs failed to state a federal antitrust claim); *Triple 7*, 338 F.Supp.2d at 1087 ("Plaintiff has failed to state a claim under the CPA for the same reasons discussed in connection with its Sherman Antitrust Act claim."); *R.J. Reynolds Tobacco Co. v. Philip Morris Inc.*, 199 F.Supp.2d 362, 396 (M.D.N.C. 2002) ("Because Plaintiffs do not allege any facts that suggest that Defendant's conduct is unlawful beyond the conduct that is the basis for their failed federal claims, Plaintiffs' state common law and statutory claims fail as well.");

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For the reasons stated above, therefore, Count Two of the SCAC is DISMISSED.

C. The Unjust Enrichment Count

Count Three of the SCAC alleges unjust enrichment: "The economic benefit of the overcharges and unlawful profits sought by and derived by Defendants through charging supra competitive and artificially inflated prices for Internet Music and CDs is a direct and proximate result of Defendants' unlawful practices." (SCAC ¶ 141; *see also* Pls.' Opp'n 40 ("[T]he economic benefit gained by Defendants from Plaintiffs through Defendants' price-fixing and anti-competitive conduct is precisely the issue here. The proper focus is on the amounts by which Defendants were enriched." (emphasis in original)).) Having concluded above that the SCAC fails to allege a violation of the antitrust laws, Plaintiffs cannot now maintain their unjust enrichment claim predicated on the benefit accruing to Defendants as a result of that alleged violation. Therefore, Count Three of the SCAC is DISMISSED.

*CONCLUSION*

For the reasons stated above, Defendants' motion to dismiss the SCAC [dkt. no. 75] is GRANTED, and Plaintiffs' motion to amend SCAC Paragraph 99 [dkt. no. 104] is DENIED as futile. The Clerk of the Court

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*Carter v. Variflex, Inc.*, 101 F.Supp.2d 1261, 1270 (C.D. Cal. 2000) ("Thus, in light of the Court's findings under the Sherman Act, the Court finds that Variflex has failed to produce sufficient evidence to support its California unfair competition claim.").

shall mark this action closed and all pending motions denied as moot.

SO ORDERED.

## APPENDIX D

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

| | | |
|---|---|---|
| In re DIGITAL MUSIC ANTITRUST LITIGATION | : | 1:06-md-01780-LAP |
| | : | Assigned to: |
| | : | Judge Loretta A. Preska |

SECOND CONSOLIDATED AMENDED COMPLAINT

### INTRODUCTION

1. Plaintiffs Barker, Benham, Clark, Edenbaum, Hall, Hampsch, Horton, Landry, Michaud, Owens, Paschkett, Putnam, Seley, Starr and Thornton, on behalf of themselves and the classes defined herein (the "Classes"), based on information, belief and investigation of counsel, except for information based on their personal knowledge, allege as follows:

2. This action is brought by plaintiffs on behalf of all persons and entities who have paid inflated prices for music sold as digital files ("Digital Music"). The two primary means of delivery of Digital Music are: (1) online via the Internet ("Internet Music"); and (2) compact discs ("CDs").

3. Recognizing that Internet Music is a substitute for CDs and that competition in the sale of Internet Music would result in lower sales and prices for CDs, Defendants conspired to restrict the output of and fix both the prices and the terms under which Internet Music would be sold. As a result of Defendants' conspiratorial and anticompetitive conduct, plaintiffs and members of the Classes have paid more for Internet Music and CDs than they would have in a Digital Music market free from Defendants' illegal restraints of trade.

4. Defendants' conduct violates, *inter alia*, the Sherman Act, state antitrust, unfair competition and consumer protection statutes, and the common law. Plaintiffs seek an order enjoining Defendants' anticompetitive conduct and damages for themselves and the Classes as a result of Defendants' unlawful conduct.

## PARTIES

5. Plaintiff Claire Barker ("Barker") is a resident of the State of Massachusetts, Suffolk County. Plaintiff Barker has purchased numerous CDs, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period (defined herein). As a result of Defendants' unlawful conduct alleged herein, plaintiff Barker has suffered injury in fact and paid artificially inflated prices for CDs.

6. Plaintiff Richard Benham ("Benham") is a resident of the State of Minnesota, Hennepin County. Plaintiff Benham has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period (defined herein). As a result of Defendants' unlawful conduct alleged

herein, plaintiff Benham has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

7. Plaintiff Sheri Clark ("Clark") is a resident of the State of California, San Diego County. Plaintiff Clark has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Clark has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

8. Plaintiff Andrew Edenbaum ("Edenbaum") is a resident of the State of Florida, Broward County. Plaintiff Edenbaum has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period (defined herein). As a result of Defendants' unlawful conduct alleged herein, plaintiff Edenbaum has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

9. Plaintiff Rachael Hall ("Hall") is a resident of the State of Florida, Leon County. Plaintiff Hall has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period (defined herein). As a result of Defendants' unlawful conduct alleged herein, plaintiff Hall has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

10. Plaintiff Paul Hampsch ("Hampsch") is a resident of the State of Hawaii, Hawaii County. Plaintiff Hampsch has purchased Internet Music, as well as numerous CDs, produced/licensed, distrib-

uted and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Hampsch has suffered injury in fact and paid artificially inflated prices for Internet Music and CDs.

11. Plaintiff Mitchell Horton ("Horton") is a resident of the State of New Mexico, Curry County. Plaintiff Horton has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Horton has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

12. Plaintiff Keaton Landry ("Landry") is a resident of the State of California, San Diego County. Plaintiff Landry has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Landry has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

13 Plaintiff Christopher Michaud ("Michaud") is a resident of the State of New York, Kings County. Plaintiff Michaud has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Michaud has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

14. Plaintiff Lisa Owens ("Owens") is a resident of the State of California, Orange County. Plaintiff Owens has purchased numerous CDs, as

well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Owens has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

15. Plaintiff David Paschkett ("Paschkett") is a resident of the State of Michigan, Genesee County. Plaintiff Paschkett has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Paschkett has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

16. Plaintiff Matthew Putnam ("Putnam") is a resident of the State of California, San Diego County. Plaintiff Putnam has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Putnam has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

17. Plaintiff Cynthia Seley ("Seley") is a resident of the State of California, Monterey County. Plaintiff Seley has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Seley has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

18. Plaintiff Kevin Starr ("Starr") is a resident of the State of Oregon, Multnomah County. Plaintiff

Starr has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Starr has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

19. Plaintiff Cato Thornton ("Thornton") is a resident of the State of California, Alameda County. Plaintiff Thornton has purchased numerous CDs, as well as Internet Music, produced, licensed, distributed and/or sold by one or more of the Defendants, during the Class Period. As a result of Defendants' unlawful conduct alleged herein, plaintiff Thornton has suffered injury in fact and paid artificially inflated prices for CDs and Internet Music.

20. Plaintiffs Barker, Benham, Clark, Edenbaum, Hall, Hampsch, Horton, Landry, Michaud, Owens, Paschkett, Putnam, Seley, Starr and Thornton are collectively referred to as ("plaintiffs").

21. Defendant Sony BMG Music Entertainment ("Sony BMG"), is a Delaware general partnership, with its principal place of business in New York and a major corporate office in Santa Monica, California. Defendant Sony BMG was formed as a joint venture of defendant Sony Corporation and Bertelsmann AG to operate their merged music operations. In or about August 2004, Defendants Sony and Bertelsmann merged their United States music operations and purportedly transferred their respective musical copyrights, licensing agreements and royalty rights to defendant Sony BMG, which is organized under the laws of New York. As a result of its formation, Sony BMG now owns and controls music re-

leased under such record labels as Arista, Columbia, Epic, and RCA Records. Defendant Sony BMG produces, licenses and distributes Internet Music and CDs through a wide variety of retailers, some of whom are owned and/or controlled by defendant Sony BMG or their corporate parents, Defendants Sony and Bertelsmann.

22. Defendant Bertelsmann, Inc. ("Bertelsmann"), is a Delaware corporation with its principal place of business in New York, and is the United States subsidiary of co-conspirator Bertelsmann AG, whose headquarters is in Gütersloh, Germany. Bertelsmann AG also owns dozens of radio and television stations in Europe; major book publishers including Random House, Bantam-Dell, Crown, Fodor's, Ballantine, Doubleday, and Knopf; direct mail media sellers Columbia House and BMG Music Service; and major magazines such as Family Circle, Parents, and YM.

23. Defendant Sony Corporation of America ("Sony"), is a New York corporation with its principal place of business in New York, and is the United States subsidiary of Sony Corporation, which is based in Tokyo, Japan. In addition to its music operations and well-known electronics business, Sony also owns many other media properties including Sony Pictures Entertainment and Columbia TriStar Pictures. Defendant Sony is a corporate parent of defendant Sony BMG Music Entertainment.

24. Defendant Universal Music Group Recordings, Inc. ("UMG"), is a Delaware corporation with its headquarters in Santa Monica, California. Defendant UMG is a subsidiary of Vivendi Universal S.A., headquartered in Paris, France. Vivendi is a conglomerate that in addition to its music business,

owns many of the leading media and telecommunication companies in Europe and Africa and is also one of the world's largest video game developers. UMG owns and controls music sold under such record labels as Mercury, Interscope, Geffen, A&M, Island Def Jam, Philips and Polydor Records. Defendant UMG produces, licenses, and distributes Internet Music and CDs through a wide variety of retailers, some of whom are owned and/or controlled by defendant UMG.

25. Defendant Time Warner, Inc. ("Time Warner") is the largest media conglomerate in the world, with its headquarters in New York, New York. It owns America Online ("AOL"), CompuServe, Netscape, MapQuest, the Atlanta Braves, HBO, CNN, Court TV, TBS, TNT, the WB Network, Turner Classic Movies, Cartoon Network, Time Warner Cable, Road Runner Hi-Speed Internet, New Line Cinema, Warner Brothers Studios, Castle Rock Entertainment, Hanna-Barbera, Warner Books, Time Life, Little Brown, Sports Illustrated, Fortune, Money, People, Entertainment Weekly, Southern Living, Field & Stream, Golf Magazine, DC Comics, and Warner Brothers Theme Parks.

26. Time Warner sold its music assets on or about March 1, 2004 to a group of investors ("WMG Investor Group"), though retaining the right to buy back part of the company. Time Warner is liable for antitrust violations of Defendant Warner Music Group ("WMG") from January 1, 1999 to the date it transferred ownership to the WMG Investor Group.

27. Defendant Warner Music Group Corp. ("WMG") is a Delaware corporation with its principal corporate headquarters located in New York, New York. WMG has since March 1, 2004 been the alter

ego of Thomas H. Lee Partners, L.P.; Bath Capital, LLC; Providence Equity Partners, Inc.; Music Capital Partners, L.P.; and Edgar Bronfman Jr. (collectively "WMG Investor Group").

28. WMG Investor Group purchased Defendant Warner Music Group from Time Warner on or about March 1, 2004. WMG Investor Group concentrated assets in itself, while concentrated liabilities in WMG. WMG reported a net loss on its most recent financial report, but would have been profitable but for the payments on its new high-interest debt. All conduct alleged as to WMG that occurred before March 1, 2004 are also alleged against Time Warner.

29. Defendant Capitol Records, Inc. ("Capitol"), a Delaware corporation; Defendant Capitol-EMI Music ("Capitol EMI"), a Delaware corporation; Defendant EMI Group North America, Inc. ("EMI North America"), a Delaware corporation; and Defendant Virgin Records America, Inc. ("Virgin"), a Delaware corporation are subsidiaries of co-conspirator EMI Group, PLC ("EMI Group"), an English corporation headquartered in London, England.

30. EMI operates in over 25 countries. At various times, EMI has signed and released music from The Beatles, The Beach Boys, The Byrds, The Hollies, and Pink Floyd. EMI produces, licenses and distributes Internet Music and CDs through a wide variety of retailers at least one of whom is owned and/or controlled by EMI.

31. Defendants, directly or through a division, parent, subsidiary, co-conspirator or agent, have had actual knowledge of, and have knowingly participated in, the conspiracy to fix the prices for Internet Music and CDs, including the restraint of the availability and distribution of Internet Music.

32. The acts charged in this Second Consolidated Amended Complaint ("Complaint") attributable to Defendants were authorized, ordered, and done by its officers, employees, agents, members or representatives while actively engaged in the management, direction, control or transaction of the business or affairs of each of the Defendants.

## OTHER CO-CONSPIRATORS

33. Co-conspirator Recording Industry Association of America (the "RIAA") is a trade organization claiming to represent companies that "create, manufacture and/or distribute approximately 90% of all legitimate sound recordings produced and sold in the United States." It is located at 1330 Connecticut Avenue, NW, Suite 300, Washington, DC 20036. The RIAA lobbies on behalf of the industry and represents its members in litigation.

34. Defendants provide a majority of RIAA's budget and the majority of its board of directors are employees of the Defendants. RIAA is controlled by the Defendants and has conspired with Defendants and participated in the illegal activities described herein. The self-described function of the RIAA "is to foster a business and legal climate that supports and promotes our members' creative and financial vitality." In fact, the RIAA provided and provides Defendants with a forum to exchange competitive information, and fix prices and terms under which Digital Music is sold.

35. Various other persons, firms, corporations, or joint ventures not named Defendants in this lawsuit, the identities of which are presently unknown, may have participated as co-conspirators with each of the Defendants' illegal activities in this Complaint and have performed acts and made statements in

furtherance of the illegal combination and conspiracy.

## JURISDICTION AND VENUE

36. Jurisdiction is conferred upon this judicial district pursuant to the Clayton Act, 15 U.S.C. §§4, 15, 16 and 26, and 28 U.S.C. §§1331 and 1337.

37. This Court also has diversity jurisdiction over the Classes pursuant to 28 U.S.C. §§1332(d)(2) and (6) of the Class Action Fairness Act of 2005 because one or more members of the Classes defined herein are citizens of a state different from one or more Defendants and the aggregate amount in controversy exceeds five million dollars, exclusive of interest and costs.

38. Venue is proper in this district pursuant to the Clayton Act, 15 U.S.C. §§4, 12, 15, 16, 22 and 26, and 28 U.S.C. §1391 because Defendants transact business in this district, and because thousands of Class members are located in this district. Additionally, a substantial part of the interstate trade and commerce involved and affected by the alleged violations of the antitrust laws was and is carried on in part within this district. The acts complained of have had, and will have, substantial anticompetitive effects in this district. Venue is proper in this district for pretrial purposes only in accordance with a transfer order issued by the Judicial Panel on Multidistrict Litigation on August 16, 2006, pursuant to 28 U.S.C. §1407. By filing this consolidated complaint, plaintiffs do not waive their right under 28 U.S.C. §1407, as recognized by the United States Supreme Court in *Lexecon Inc. v. Milberg Weiss Bershad Hynes & Lerach*, 523 U.S. 26 (1998) to return to the respective district from which they were trans-

ferred at the conclusion of pretrial proceedings in this Court.

## TRADE AND COMMERCE

39. During the Class Period, each of the Defendants, itself or through its affiliates, agents or subsidiaries, produced, licensed, distributed and/or sold Digital Music in a continuous and uninterrupted flow of intrastate and interstate commerce throughout the United States.

## RELEVANT MARKET

40. As to claims so requiring, the relevant product market for purposes of this action is the market for sales of Digital Music. The relevant geographic market is the United States. Defendants function as a collusive oligopoly. Defendants are the four largest music labels and control in excess of 80% of the market for all sales of Digital Music in the United States. Jointly, they exercise market power over and dominate the market for Digital Music.

41. Internet Music and CDs are viewed as substitutes by both record labels and consumers as evidenced by the inverse relationship between sales of CDs and Internet Music. Internet Music and CDs are reasonably interchangeable because: (1) both CDs and Internet Music can be played on a computer; (2) Internet Music can be converted into CDs, though Defendants have at times colluded to place terms on consumers restricting this ability; (3) Digital Music purchased in either form may be played on digital music players; (4) most Digital Music is purchased by consumers who have means of playing both Internet Music and CDs; (5) they are simply different delivery methods of identical subject matter; and (6) both forms of Digital Music offer high audio

quality approaching or exceeding other forms of music such as broadcast radio, satellite radio, vinyl records and audiocassettes.

## CLASS ACTION ALLEGATIONS

42. Plaintiffs bring this action on behalf of themselves, and all others similarly situated, pursuant to Rule 23(b)(2) and (3) of the Federal Rules of Civil Procedure. Plaintiffs seek to represent the following Classes:

**Injunctive Relief Class**

43. All purchasers of Digital Music produced, manufactured, licensed, distributed and/or sold by Defendants in the United States (excluding federal, state and local governmental entities, Defendants, their directors, officers and members of their families).

**End Purchaser Internet Music Damages Class**

44. All persons or entities in Arizona, California, the District of Columbia, Florida, Iowa, Kansas, Maine, Massachusetts, Michigan, Minnesota, Nebraska, Nevada, New Mexico, New York, North Carolina, North Dakota, South Dakota, Tennessee, Vermont, West Virginia and Wisconsin (the "End Purchaser States") (excluding federal, state and local governmental entities, Defendants, their directors, officers and members of their families) that purchased Internet Music produced, manufactured, distributed and/or sold by Defendants from December 4, 2001 through the conclusion of the trial of this matter ("Class Period"), for their own use and not for resale, and all persons or entities in the United States (excluding federal, state and local governmental entities, Defendants, their directors, officers and mem-

bers of their families) that purchased Internet Music for their own use and not for resale directly from Defendants and/or entities owned or controlled by Defendants during the Class Period.

**End Purchaser CD Damages Class**

45. All persons or entities in the End Purchaser States (excluding federal, state and local governmental entities, Defendants, their directors, officers and members of their families) that purchased CDs produced, manufactured, distributed and/or sold by Defendants during the Class Period, for their own use and not for resale, and all persons or entities in the United States (excluding federal, state and local governmental entities, Defendants, their directors, officers and members of their families) that purchased CDs for their own use and not for resale directly from Defendants and/or entities owned or controlled by Defendants during the Class Period.

46. Excluded from each of the Classes are Defendants, their directors, officers and members of their families; any entity which any defendant owns, controls or has controlling interest; the affiliates, legal representatives, attorneys, heirs or assigns of any defendant; and any federal, state or local governmental entity.

47. The Classes are so numerous that joinder of all members is impracticable. There are thousands of members in the Classes who are geographically dispersed throughout the United States and the End Purchaser States.

48. Plaintiffs' claims are typical of the claims of the members of the Classes because plaintiffs and all Class members were damaged by the same wrongful conduct of the Defendants alleged herein.

49. Plaintiffs' claims are typical of the claims of the members of the Classes because the substantive legal standards that Defendants are subject to are substantially the same.

50. There are questions of law and fact common to the Classes which predominate over any questions affecting only individual Class members. Such common questions include:

(a) Whether the Defendants violated the Sherman Act and relevant End Purchaser State-antitrust and consumer protection statutes, which subject Defendants to substantially the same legal standards, by engaging in a continuing combination and conspiracy to restrain the availability and distribution of and fix the prices for Internet Music and, as a result, maintain the prices for CDs at supra-competitive levels;

(b) The duration and extent of any such combination or conspiracy alleged;

(c) Whether the Defendants and each of them were participants in any such combination or conspiracy alleged herein;

(d) Whether Defendants fixed the price of Internet Music at supracompetitive levels;

(e) Whether Defendants conspired to impose restrictive terms concerning the purchase and use of Internet Music;

(f) Whether Plaintiffs and members of the classes paid supracompetitive prices for CDs; and/or

(g) Whether Defendants' conduct caused damage to plaintiffs and members of the Classes, and if so, the appropriate measure of such damages.

51. The claims of the plaintiffs are typical of the claims of the Classes, and plaintiffs have no interest adverse to the interest of other members of the Classes.

52. Plaintiffs will fairly and adequately protect the interests of the Classes and have retained counsel experienced and competent in the prosecution of complex class actions and antitrust litigation.

53. To the extent that any plaintiff is not adequate, plaintiffs reserve the right to add a plaintiff or Class representative.

54. A class action is superior to other available methods for the fair and efficient adjudication of the controversy. Such treatment will permit a large number of similarly situated persons to prosecute their common claims in a single forum simultaneously, efficiently, and without duplication of effort and expense that numerous individual actions would engender. Class treatment will also permit the adjudication of relatively small claims by many Class members who could not afford to individually litigate an antitrust claim against large corporate Defendants. There are no difficulties likely to be encountered in the management of this class action that would preclude its maintenance as a class action, and no superior alternative exists for the fair and efficient adjudication of the controversy.

55. Defendants have acted on grounds generally applicable to the entire Class, thereby making final injunctive relief or corresponding declaratory relief appropriate with respect to the Class as a whole.

## FACTUAL BACKGROUND OF DEFENDANTS' ANTICOMPETITIVE CONDUCT

56. Defendants produce, license and distribute Digital Music, including Internet Music and CDs, to retailers for sale throughout the United States and in some instances sell Internet Music and CDs directly to consumers through Internet sites, record clubs and other entities which they own or control.

57. Defendants produce, license and distribute Digital Music, including Internet Music and CDs, to retailers for sale throughout the United States and in some instances sell Internet Music and CDs directly to consumers through Internet sites, record clubs and other entities which they own or control.

58. Defendants Bertelsmann, EMI, Sony, and WMG sold music directly to consumers over the Internet through their MusicNet joint venture.

59. Defendants Sony and UMG sold Internet Music directly to consumers through their joint venture, pressplay.

60. Defendant Sony sells and has sold Internet Music directly to consumers using, *inter alia*, its online store, Sony Connect.

61. Defendant Sony BMG sells and has sold CDs to consumers directly on Sony Music Store and other channels.

62. Defendant BMG sells and has sold CDs directly to consumers through its BMG Music Club service.

63. Defendant WMG sells and has sold CDs and Internet Music directly to consumers.

64. In 2005, defendant BMG's corporate parent Bertelsmann AG acquired Columbia House, BMG Music Club Service's only major record club competitor in the United States, through which it sells and has sold CDs directly to consumers.

65. Defendant Time Warner sells and has sold Internet Music to consumers directly on its online store AOL Music Now, and sells CDs directly to consumers using AOL Music and through other channels.

**Overview of Antitrust Claims and Nature of the Conspiracy**

66. The Defendants and their co-conspirators have engaged in a continuing conspiracy to restrain the availability and distribution of Internet Music, fix and maintain at artificially high and non-competitive levels the prices at which they sell such music, impose unreasonable restrictive terms in the purchase and use of such music and limit the quantities of such music sold. By restraining trade in and fixing the price of Internet Music, Defendants were able to sell CDs at supracompetitive prices.

67. The conspiracy has had several aspects and stages. At the outset, Bertelsmann, WMG, and EMI agreed to launch a service called "MusicNet" and UMG and Sony agreed to launch a service called "Duet," which was later renamed "pressplay." During the class period, MusicNet was co-owned and controlled by various defendants, including WMG, Sony BMG and EMI. Eventually all the Defendants signed distribution agreements with MusicNet and pressplay. These ventures maintained prices at artificially high levels, eliminated competition among the Defendants in the pricing and terms of Internet Music sales and provided one of several forums in

which the Defendants could discuss their general desires to restrain trade in Internet Music and come to agreement on the specifics.

68. Defendants have also agreed to exchange price information and terms of sale information for Internet Music; and came to revenue sharing agreements and agreed among each other to use "Most Favored Nation" clauses (MFNs). These and other anticompetitive agreements served and were intended to serve to limit competition among the Defendants.

69. In addition, when Defendants eventually sold Internet Music directly to retailers who, unlike pressplay and MusicNet, they did not control, they did not compete independently. Instead, they agreed to fix the terms of sale, including digital rights management ("DRM") and the prices at which they were sold.

**History of the Conspiracy and Its Constituent Agreements**

70. Internet Music has the potential to transform the market for Digital Music by increasing the selection of music that can be distributed while dramatically reducing costs associated with production, distribution and sale through the now traditional medium of CDs.

71. Pricing for CDs accounts for costs such as producing master discs; producing copies of the disc; the CD case; labels and anti-shoplifting packaging; shipping CDs to distribution warehouses and then to record stores; labor to unpack and shelve the CDs, staff cash registers, and other retail overhead costs; and returning and destroying damaged and unsold inventory. All of these costs are eliminated when

music is distributed via digital downloads from the Internet.

72. As discussed previously, Defendants launched two Internet Music distribution services in late 2001. Bertelsmann, WMG, and EMI agreed with each other to launch, and did in fact launch, a service called "MusicNet;" and UMG and Sony agreed with each other to launch, and did in fact launch a service called "Duet," which was later renamed "pressplay." Eventually all of the Defendants signed distribution agreements with MusicNet and pressplay, thereby creating an agreement of all Defendants to distribute music on the terms and at the prices determined by MusicNet and pressplay.

73. Defendants, via exchange of pricing information, terms of sale information, revenue sharing agreements, MFN's and other anticompetitive conduct conspired to fix the prices, quality and terms under which Internet Music would be sold.

74. As a general rule in competitive markets, dramatic cost reductions such as those associated with Internet Music distribution are accompanied by dramatic price reductions and output expansion. Absent Defendants' anticompetitive conduct, including the agreements to restrain competition among themselves, Internet Music would be dramatically less expensive than CDs. Instead, despite lower costs, the labels conspired to restrain output and charge more money for Internet Music and to provide lower quality music, well below CD-quality, which is further hampered by DRM.

75. In order to be able to choose music from all major record labels and thereby have access to the music generally available on CDs, a consumer initially would have had to subscribe to both pressplay

and MusicNet, at a cost of approximately $240 per year. A consumer who attempted to write music onto CDs from pressplay was limited to only certain songs and no more than two songs from any particular artist per month. Even worse, Internet Music purchased from the Defendants often would "expire" unless repurchased. For example, with MusicNet, the amount of music contained on a normal CD would cost $20 per year to purchase (more than an average CD), and yet after that year, the consumer would need to repurchase the music for an additional $20 for another year's access. If a consumer tried to unsubscribe from a service such as pressplay, he or she would immediately lose access and be unable to play all the music that he or she had "purchased."

76. MusicNet and pressplay did not allow transfer of the songs to portable digital music players such as the iPod, eliminating one of the main reasons for consumers to purchase music in this format. The Defendants adhered to this very unpopular DRM and were not competing in transferability terms as they would have absent the conspiracy complained of herein. Any one of the Defendants might have removed these unpopular DRM and gained additional market share and profits and most or all would have but for the conspiracy, just as independent labels not party to the conspiracy sell DRM-free Internet Music via eMusic.

77. Industry commentators stated that "[a]t the proposed prices, it is difficult to fathom how pressplay and MusicNet will be able to compete . . . . The problem is MusicNet and pressplay do not offer

reasonable prices."[1] One prominent computer industry magazine noted that "nobody in their right mind will want to use" the services.[2]

78. Such high prices would not occur after the introduction of a ***lower cost distribution*** system absent an agreement to restrain trade and keep prices high. In an industry free of collusion, an innovation that lowers a company's variable costs, which include distribution costs, will result in a company lowering its prices and. passing on a part of the savings to the consumer. This partial pass on allows the company to increase its market share while increasing its profit margin because not all of the decreased cost is passed on. Instead, rather than pursue their individual interests by competing with each other, the new method of distribution was used as a pretext for Defendants to meet and conspire.

79. Eventually Defendants and their joint ventures sold Internet Music to consumers through entities they did not own or control. However, they could only do so if they contracted with MusicNet to provide Internet Music for the same prices and with the same restrictions as MusicNet itself and other MusicNet licensees. Defendants imposed terms on licensees that forced them to pay penalties in the form of higher prices for Defendants' music or even termi-

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[1] *See* Richard Menta, *PressPlay and MusicNet to Launch*, MP3newswire.net, September 17, 2001, available at http://www.mp3newswire.net/hyperlink under "archived stories."

[2] *See Digital Music: Worth Buying Yet?*, PCWorld.com, January 18, 2002, available at http://www.pcworld.com/article/id,80564-page,1/article.html.

nated their licenses if the licensees attempted to license music from another company. This not only restrained trade in the Internet Music business and forestalled the time by which Internet Music would emerge as a reasonable consumer substitute for CDs, but also prevented the small independent labels that competed with Defendants from obtaining access to many outlets for Internet Music.

80. In June of 2001, MusicNet revived the then-bankrupt Napster service and forced it into such a license. Defendants Sony and UMG are or were minority shareholders in the "new" Napster. To this day, Napster's service is under many of the same restrictions as the MusicNet and pressplay services, such as the loss of access to downloaded songs once a consumer's membership expires.

81. The failure and inefficiency of these Internet Music distribution services was a direct result of the high prices and unfavorable terms the Defendants colluded to impose on purchasers of Internet Music. Defendants collectively refused to utilize or license a system that was convenient, not burdened with use restrictions and competitively priced.

82. Defendants' collusion in setting high prices for Internet Music, as well as their collusion in imposing unfair and one-sided terms on its use, made Internet Music less attractive to consumers, allowing Defendants to sell CDs at supracompetitive prices.

83. Acting alone, no defendant could sustain the supracompetitive prices for CDs prevailing in the CD market. This inability to charge high CD prices, as market factors made consumer demand for CDs more elastic over time at the prices charged by Defendants during the conspiracy, gave Defendants motive to conspire.

84. Defendants' collusion further allows them to engage in the anticompetitive practice of tying or "bundling" Internet Music onto a single online "album."

85. Roger Noll, a well-respected economist and Professor at Stanford University, has characterized the Defendants' conduct as follows:

> The main findings and conclusions of this essay are as follows: First, the five distribution companies have created several joint ventures. The two most important joint ventures are MusicNet (BMG, EMI and Warner each owned 20 percent, and Real Networks the remaining 40 percent) and pressplay (owned by Sony and Universal), both of which engage in the wholesale and retail digital distribution of recorded music. Second, if public information about these two joint ventures is accurate, each will set wholesale prices for digitally distributed recordings that are controlled by their affiliated distribution companies, while pressplay also will set retail prices, so that ***both ventures constitute horizontal price-fixing agreements***. Third, if information in the public record is accurate, ***these five companies apparently have engaged in vertical foreclosure*** by refusing to enter into agreements on reasonable terms with other entities for digital distribution of their library of recordings and by imposing unnecessary burdensome licensing requirements on both retail competitors and their customers. Fourth, in the period immediately before and during the evolution of the policies of these

> companies regarding digital distribution, ***these five companies engaged in anti-competitive activities that have led to several adverse antitrust rulings by competition policy agencies in the United States and abroad.***[3]
>
> If the information in the public record that forms the basis of these conclusions is accurate, the joint ventures for digital distribution of recorded music are anticompetitive horizontal combinations, and the vertical restraints imposed by the distribution companies are also anticompetitive. The effects of these anticompetitive acts will be to reduce or even to eliminate the number of independent competitors in both wholesale and retail digital distribution, and thereby to harm consumers by raising prices and increasing price discrimination, and to harm artists by reducing competition for the right to distribute their recordings. Thus, the joint ventures and vertical foreclosure activities, if accurately reported, constitute misuse of the copyrights that are controlled by the distribution companies, their corporate affiliates, and other publishers.

Roger G. Noll, *Napster's Copyright Abuse Defense* (presented to University of Texas Law School Colloquium on Information and Communication Policy), March 24, 2003, available at www.utexas.edu/law/news/colloquium/archive/2003springsched.html, un-

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[3] Emphasis is added and citations are omitted here and throughout, unless otherwise noted.

der hyperlink "Napster's Copyright Abuse Defense" at 2.

86. Defendant Edgar Bronfman, Jr., who is currently CEO of WMG, in his prior capacity as Executive Vice Chairman of Vivendi Universal and the UMG executive in charge of his company's role in pressplay reportedly described pressplay as follows:

> "Pressplay has what we call an affiliate model where ***we determine the price***, and we offer a percentage of that price to the retailing partner, in this case either Microsoft or Yahoo or MP3. The reason we've chosen that, frankly, ***is because we are concerned that the continuing devaluation of music will proceed unabated unless we do something about it***. If you allow an AOL or RealNetworks or Microsoft or others, who have very different business models, to use music to promote their own business model and simply pay the artists and record companies the minimums, they can advantage themselves on the back of the music industry in a way which continues to devalue music."

Cited in Noll, Napster's Copyright Abuse Defense, *id.* at 27.

87. The MusicNet and pressplay joint ventures provided Defendants with opportunities and forums to meet and further conspire to cooperate to maintain the prices and terms for Internet music. In antitrust claims brought by investors and creditors of the bankrupt Napster against several of the Defendants, the Honorable Marilyn Hall Patel wrote, "even a naif must realize that in forming and operating a joint venture, [record label] representatives must necessarily meet and discuss pricing and li-

censing. . . [t]hese joint ventures bear the indicia of entities designed to allow [record labels] to use their copyrights and extensive market-power to dominate the market for digital music distribution. Even on the undeveloped record before the court, these joint ventures look bad, sound bad and smell bad."[4]

88. In addition, the main industry trade association, the RIAA, which is controlled by the Defendants, provides another forum and means through which Defendants can communicate about the pricing, terms and use restrictions they collectively agree upon with respect to Internet Music.

89. Defendants were paid shares of the total revenue generated by a joint venture licensee rather than by receiving money on a per song basis. Each Defendants' financial interest in the joint ventures was therefore linked to the total sales of all the labels rather than its own market share. By doing so Defendants agreed to structure and did in fact structure the joint ventures such that their economic incentives were to charge monopoly prices for Internet Music rather than compete with one another on price.

90. In addition to sharing information that violated the purported independence of these joint ventures, Defendants conspired to mask their anticompetitive conduct by pretextually establishing rules to prevent antitrust violations, ignoring them, and then using these sham rules to convince the United States

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4 *In re Napster, Inc. Copyright Litig.*, 191 F. Supp. 2d 1087, 1109 (N.D. Cal. 2002).

Department of Justice ("DOJ") to drop the investigation it launched in 2001.

91. In "White Papers" presented to the DOJ, Defendants claimed they had instituted firewalls, communication guidelines, safeguards, and other supposed protections to prevent exchanges of information, or other conduct, that could negatively affect competition.

92. Defendants also had and have a common practice of using MFNs in their licenses that had the effect of guaranteeing that the licensor would receive terms that were no less favorable than the terms offered to other licensors.

93. Defendants attempted to hide the MFNs and communications between the joint ventures and their label owners because they knew they would attract antitrust scrutiny by DOJ and others.

94. For example, EMI and MusicNet had a "side letter" agreement which assured that EMI's core economic terms would be no less favorable than Bertelsmann's and WMG's.

95. EMI CEO Rob Glaser decided to put the MFN in a secret side letter because "there are legal/antitrust reasons why it would be bad idea to have MFN clauses in any, or certainly all, of these agreements."

96. UMG also made use of MFN clauses in its license agreements.

97. When Defendants use MFN clauses, the result is that Defendants gets the benefit of any one negotiation by a competitor. In a January 12, 2006 article, the Wall Street Journal confirmed that MFN clauses are used by Defendants. In the same article,

Johnathan Potter, executive director of Digital-Media Association, (the trade organization that represents digital music providers including Napster, AOL, Apple, MSN, and RealNetworks) stated that "seller-side MFNs are inherently price-increasing and anticompetitive."

98. In sum, MusicNet and pressplay were vehicles through which the Defendants effectively exchanged price information, policed their cartel and imposed restrictive licensing arrangements that retarded the growth of Internet Music. Defendants have maintained a price floor for Internet Music throughout the period of their collusion, even as the prices of other products and Defendants' own variable costs have varied.

99. Defendants continued to engage in anticompetitive acts designed to inhibit competition after services other than their joint ventures began to distribute Internet Music. In this vein, Defendants have agreed to a wholesale price floor whereby they sell Internet Music to retailers at or about 70 cents per song. Defendants enforce their price floor in part by forcing Internet Music retailers to sign MFN agreements that specify that the retailers must pay each of the Defendants the same amount.

100. By setting a wholesale price floor at 70 cents per song, Defendants have fixed and maintained the price of Internet Music at supracompetitive levels. In addition, they have placed restrictions on the use of Internet Music that unreasonably limit its utility and attractiveness to purchasers.

101. The relative market shares of the Defendants have been largely fixed over the period of their conspiracy. Given that the independent labels are not party to Defendants' collusive agreements, their

market share relative to the market share of Defendants has increased.

102. Absent an agreement not to compete with each other, Defendants would try to gain advantages over each other by selling Internet Music with fewer unpopular restrictions; hence the lack of such competition on price or quality shows continuing collusion.

103. To illuminate the price and terms of Internet Music absent collusion, and to assess the impact of Defendants' anticompetitive conduct, one need only look at eMusic, the most popular online music service that sells Internet Music owned by independent labels. eMusic charges $10 for 40 songs, or $0.25 per song, and places ***no restrictions*** on how purchasers may upload their music to iPods, upload to other digital music players, or burn to CDs. By contrast, Defendants' collusive wholesale price is more than double the eMusic $0.25 retail price.

104. Defendants' response to the challenge of eMusic was to refuse to do business with eMusic, which was the first major Internet Music retailer. Acting against their individual self interest, none of the Defendants have joined the hundreds of independent record labels that have a successful relationships with eMusic, which has grown to become the #2 Internet Music retailer, behind only Apple, Inc.'s iTunes Store. Nearly all of the independent record labels, unlike the Defendants, sell their music on both iTunes Store and eMusic.

105. By conspiring to restrain the growth of Internet Music through the imposition of restrictive terms of use and to set a price floor for Internet Music at supracompetitive levels, Defendants have protected their ability to maintain sales of CDs at prices

higher than they would be but for Defendants' anti-competitive conduct.

106. Defendants' price fixing is the subject of a pending investigation by the Office of the New York State Attorney General ("New York State Attorney General") who subpoenaed Defendants for information on the wholesale prices they charge for Internet Music.

107. On March 3, 2006, the DOJ opened an investigation into collusion and price fixing of Internet Music by the Defendants.

108. The Defendants either have received or will soon receive formal "civil investigation demands," which are similar to subpoenas, from the DOJ.

109. Defendants are no strangers to lawsuits and government investigations for anticompetitive behavior related to the terms of sales and the pricing of Digital Music.

110. For example, Defendants were subject to a number of government investigations and lawsuits concerning the pricing of CDs. There is also an investigation into whether Defendants misled the DOJ into the formation and operation of MusicNet and pressplay.

111. In another example of recent anticompetitive behavior, the New York State Attorney General and the Federal Communications Commission found exhaustive evidence of illegal "payola" schemes of paying radio stations for playing certain songs, an illegal practice that locks out new artists and smaller record companies. Defendants entered into settlements in 2006 and 2007 totaling more than $29 million and have all signed extensive agreements to in-

stitute monitoring protocols to prevent future violations of the law from remaining undetected.

112. Regarding the intent to cover up their illegal payments, a press release from the New York State Attorney General noted that documents revealed by its investigation showed how record label employees "took steps to conceal many of the payments to individuals and radio stations, by using fictitious 'contest winners' to document the transactions and make it appear as though the payments and gifts were going to radio listeners instead of station employees." Office of the New York State Attorney General Press Release, *Sony Settles Payola Investigation: Company Acknowledges Problems, Agrees to Sweeping Reforms*, July 25, 2005.

**Fraudulent Concealment**

113. Throughout the relevant period, Defendants and their co-conspirators affirmatively and fraudulently concealed their unlawful conduct from plaintiffs.

114. Defendants' illegal activities are by their nature inherently self-concealing.

115. Only on or about March 3, 2006, when the Department of Justice opened an investigation into collusion and price fixing of Internet Music by the Defendants, was the existence of the conspiracy disclosed to the public. Plaintiffs could not have discovered the unlawful conduct at an earlier date through the exercise of reasonable diligence because of Defendants' and their co-conspirator's active and purposeful concealment of their unlawful activities.

116. Defendants and their co-conspirators engaged in an illegal price-fixing conspiracy with re-

spect to Internet Music, which they affirmatively concealed, in at least the following respects:

(a) by meeting secretly to discuss the prices of Internet Music;

(b) by agreeing among themselves at meetings and in communications not to discuss publicly, or otherwise reveal, the nature and substance of the acts and communications in furtherance of their illegal scheme;

(c) by giving false and pretextual reasons for their unlawful activities; and

(d) by masking their unlawful activities behind the cover of joint ventures and trade associations.

(e) By colluding to and in fact making false statements in two "White Papers" submitted to the United States Department of Justice relating to claimed "safeguards" preventing the exchange of Defendants' competitively sensitive information in the operation of MusieNet and pressplay.

117. Defendants concealed their illegal price-fixing conspiracy with the intention of inducing Plaintiffs and class members to purchase Digital Music at supracompetitive prices.

118. Defendants signed distribution agreements with MusicNet and pressplay. These ventures maintained Internet Music prices at artificially high levels, eliminated competition among the Defendants in the pricing and terms of Internet Music sales and provided one of several forums in which the Defendants could discuss their general desires to restrain trade in Internet Music and come to agreement on the specifics.

119. In addition, Defendants agreed to exchange price information, exchange terms of sale information, came to revenue sharing agreements, and agreed among each other to use "Most Favored Nation" clauses (MFNs). These and other anticompetitive agreements served and were intended to serve to limit competition among the Defendants.

120. In addition, when Defendants eventually sold directly to retailers who unlike pressplay and MusicNet they did not control, they did not compete independently. Instead they agreed to fix the terms of sale, including DRM specifications and the prices at which they sold. Plaintiffs did not discover, and could not have discovered through the exercise of reasonable diligence; that: Defendants and their co-conspirators were violating the antitrust laws as alleged herein until shortly before this litigation was commenced, nor could Plaintiffs have discovered the violations earlier than that time because Defendants and their co-conspirators conducted their conspiracy in secret, concealed the nature of their unlawful conduct and acts in furtherance thereof, attempted to confine information concerning the combination and conspiracy and fraudulently concealed their activities through various other means and methods designed to avoid detection.

121. As a direct result of the representations and concealments made by Defendants, Plaintiffs believed and relied upon them, and were thereby induced to pay supracompetitive prices for Digital Music.

122. As a result of Defendants' and their co-conspirators' fraudulent concealment of their conspiracy, plaintiff asserts the tolling of any otherwise-applicable statute of limitations.

## COUNT I

### For Violation of Section 1 of the Sherman Act (On Behalf of All Classes)

123. Plaintiffs reallege and incorporate by reference each and every allegation set forth above. This Count is brought pursuant to 15 U.S.C. § 1 and 15 U.S.C. § 16, for injunctive relief as to the Injunctive Relief Class, and for damages for members of the End Purchaser Internet Music Damages Class and End Purchaser CD Damages Class, who purchased Internet Music and/or CDs directly from Defendants and/or entities controlled by Defendants.

124. The Digital Music market is dominated by four entities – Defendants EMI, Sony BMG, UMG and WMG – which collectively function as a highly concentrated, tightly-knit oligopoly. Together, Defendants account for over 80% of Digital Music sold to End Purchasers in the United States. The relatively few firms have created an industry environment which enables and facilitates Defendants' ability to coordinate their pricing and other practices such as DRM and the other restrictions on Internet Music. These agreements explain the market share stability in this industry which could not be fully explained absent an agreement not to compete particularly when this industry has been subject to sweeping advancements in technology and changes in public taste and fashion for music.

125. The Digital Music market is characterized by high barriers to entry by new firms, thus further enhancing Defendants' significant market power. The high degree of concentration in the industry and the significant barriers to entry have insulated Defendants from price competition just as their con-

spiracy has insulated them from competition from one another.

126. Beginning at least as early as December 4, 2001, the exact date being unknown to plaintiffs, and continuing to the present, Defendants and their co-conspirators have engaged in a continuing combination, conspiracy, and common course of conduct in unreasonable restraint of interstate trade and commerce in violation of §1 of the Sherman Act, 15 U.S.C. §1. As more fully described herein, the combination, conspiracy and common course of conduct engaged in by Defendants consisted of a continuing agreement, understanding and concert of action among the Defendants and their co-conspirators, the substantial terms of which were to restrain the availability and distribution of Internet Music, fix and maintain at artificially high and non-competitive levels the prices at which they sold Internet Music and impose unreasonably restrictive terms in the purchase and use of Internet Music. By restraining trade in and fixing the price of Internet Music, Defendants were able to sell at artificially high and non-competitive levels the prices at which they sold CDs. As a result of their conspiracy, combination and common course of conduct, and despite declining costs of production associated with the introduction of new technologies, Defendants sold both Internet Music and CDs at supracompetitive levels.

127. Pursuant to their combination, conspiracy and concerted action, Defendants, adopted and adhered to virtually identical and parallel methods of distribution (including the use of contracts with substantially identical material terms), pricing (including the use of lockstep, identical pricing for virtually every song in their catalogues for Internet Music)

and modes of DRM. Defendants are the pivotal and controlling link between the artistic production of the music on the one hand, and the marketing and distribution of Digital Music on the other. Defendants distribute Digital Music throughout the United States, including recordings produced under Defendants' own labels as well as recordings produced by certain independent music companies.

128. Currently Defendants sell Internet Music to retailers and distributors at or about $0.70 per song despite improvements in technology of the distribution of Internet Music and exponentially increased sales volume that have dramatically reduced marginal costs. Were Defendants to sell Internet Music at competitive prices and/or refrain from colluding to impose restrictive terms of use and purchase, they would be forced to cut prices of CDs. In consequence, Defendants' conspiracy to restrain the availability and distribution of Internet Music, and to fix and maintain the price of Internet Music, has protected the sale of CDs and enables Defendants to maintain CD prices at supracompetitive levels.

129. During the Class Period, Defendants together took actions to restrain the availability and distribution of Internet Music through their refusals to deal with independent Internet distribution services and through their attempt to control the distribution of Internet Music through their proxies, MusicNet and pressplay. Defendants adopted identical terms of sale and pricing schemes for Internet Music. Pursuant to their combination, conspiracy and concerted action, Defendants have consistently agreed to have adopted parallel-pricing schemes.

130. Defendants' current business practices are also the subject of pending investigations by the New

York State Attorney General, who subpoenaed Defendants for information on the wholesale prices they charge for Internet Music and the DOJ, which has also demanded information of Defendants.

131. Defendants have and continue to use trade associations, including the RIAA, to restrain and control the sale of Internet Music and to plan strategy and communicate pricing. During meetings of the record industry, Defendants discussed how to put Napster out of business and rein in similar threats by distributors of Internet Music to their pricing and distribution oligopoly. At a recent meeting, Defendants openly discussed adopting a variable online price scheme (*i.e.*, to charge more for certain singles and less for others).

132. Each of the Defendants has engaged in one or more overt acts in furtherance of the contract, combination and/or conspiracy alleged. In consequence, the aforesaid combination and conspiracy had the following effects, among others:

(a) Plaintiffs and other members of the Classes were deprived of the benefits of free and open competition in the purchase of Defendants' Internet Music and CDs;

(b) Defendants' Internet Music prices were raised, fixed and maintained at artificially high and non-competitive levels;

(c) Plaintiffs and other members of the Classes were forced to pay artificially high, non-competitive prices for Internet Music and CDs; and

(d) Price competition among Defendants in the sale of Internet Music, and as a direct consequence in the sale of CDs, was restrained, suppressed and eliminated.

131. During the Class Period, plaintiffs and other members of the Classes purchased substantial quantities of Internet Music and CDs sold by Defendants. By reason of the violations of §1 of the Sherman Act, plaintiffs and other members of the Classes paid more for Internet Music and CDs than they would have in the absence of the illegal combination, conspiracy and common course of conduct and, as a result, have been injured in their business and property and have suffered damages in an amount currently undetermined.

134. Defendants have acted on grounds generally applicable to the Classes, thereby making final injunctive relief appropriate with respect to the Classes as a whole.

## COUNT II

### For Violation of State Antitrust and Unfair and Deceptive Acts and Practices Statutes (On Behalf of End Purchaser Internet Music and CD Damages Classes)

135. Plaintiffs reallege and incorporate by reference each of the allegations set forth above.

136. This Count is alleged against all Defendants on behalf of the End Purchaser Internet Music and CD Damages Classes. Defendants' conduct as alleged herein violates the antitrust and/or unfair and deceptive acts and practices laws of each of the following jurisdictions:

(a) **Arizona**: The aforementioned practices by Defendants were and are in violation of the Arizona Uniform State Antitrust Act, Arizona Revised Statutes §44-1401, *et seq.*;

(b) **California**: The aforementioned practices by Defendants were and are in violation of the Cartwright Act, California Business and Professions Code §16700, *et seq.*; and the Unfair Competition Law, California Business and Professions Code §17200, *et seq.*;

(c) **District of Columbia**: The aforementioned practices by Defendants were and are in violation of the District of Columbia Antitrust Act, District of Columbia Annotated Code §28-4501, *et seq.*; and the District of Columbia Consumer Protection Act, District of Columbia Code Annotated §§28-3901, *et seq.*;

(d) **Florida**: The aforementioned practices by Defendant were and are in violation of the Florida Deceptive and Unfair Trade Practices Act, Florida Statutes §501.201, *et seq.*;

(e) **Iowa**: The aforementioned practices by Defendants were and are in violation of the Iowa Competition Law, Iowa Code §553.1, *et seq.*;

(f) **Kansas**: The aforementioned practices by Defendants were and are in violation of the Kansas Unfair Trade and Consumer Protection Act, Kansas Statutes Annotated §50- 101, *et seq.*;

(g) **Maine**: The aforementioned practices by Defendants were and are in violation of the Maine Regulation of Trade Law of 1954, Maine Revised Statutes Annotated, Title 10, §1101, *et seq.*, and the Maine Unfair Trade Practices Act, Maine Revised Statutes Annotated §205-A, *et seq.*;

(h) **Massachusetts**: The aforementioned practices by Defendants were and are in violation of the Massachusetts consumer protection act, Massachusetts General Laws, Chapter 93A, Section 2, and

are actionable under Chapter 93A, Section 9. Statutory demand has been made (pursuant to Chapter 93A Section 9(3) upon Defendants Sony BMG, Bertelsmann, Sony, UMG, and WMG, and said Defendants have failed to make a reasonable offer of relief. Plaintiffs are not alleging a violation under Mass. General Law Ch. 93A §§1 *et seq.* against defendants Capitol, Capitol-EMI, EMI North America, Time Warner, and Virgin at this time, but will be doing so once they have complied with the procedural requirements set forth in Chapter 93A §9(3).

(i) **Michigan**: The aforementioned practices by Defendants were and are in violation of the Michigan Antitrust Reform Act, Michigan Compiled Laws §445.772, *et seq.*;

(j) **Minnesota**: The aforementioned practices by Defendants were and are in violation of the Minnesota Antitrust Act of 1971, Minnesota Statutes §325D.49, *et seq.*;

(k) **Nebraska**: The aforementioned practices by Defendants were and are in violation of the Nebraska Consumer Protection Act, Nebraska Revised Statutes §59.1601, *et seq.*;

(l) **Nevada**: The aforementioned practices by Defendants were and are in violation of the Nevada Unfair Trade Practice Act, Nevada Revised Statutes §598A.010, *et seq.*;

(m) **New Mexico**: The aforementioned practices by Defendants were and are in violation of the New Mexico Antitrust Act, New Mexico Statutes Annotated §57-1-1, *et seq.*; and the New Mexico Unfair Practices Act, New Mexico Statutes Annotated §57-12-3;

(n) **New York**: The aforementioned practices by Defendants were and are in violation of The New York consumer protection act, New York General Business Law §349; and New York common law against restraints of trade. Plaintiffs do not seek treble damages, special damages or penalties under General Business Law §349;

(o) **North Carolina**: The aforementioned practices by Defendants were and are in violation of the North Carolina Unfair and Deceptive Trade Practices Act, North Carolina General Statutes §75-1, *et seq.*;

(p) **North Dakota**: The aforementioned practices by Defendants were and are in violation of North Dakota's antitrust law, North Dakota Century Code §51-08.1-01, *et seq.*;

(q) **South Dakota**: The aforementioned practices by Defendants were and are in violation of South Dakota's antitrust law, South Dakota Codified Laws §37-1-3.1, *et seq.*;

(r) **Tennessee**: The aforementioned practices by Defendants were and are in violation of the Tennessee Trade Practices Act, Tennessee Code Annotated §47-25-101, *et seq.*;

(s) **Vermont**: The aforementioned practices by Defendants were and are in violation of Vermont antitrust law, Vermont Statutes Annotated, Title 9, §245 1, *et seq.*;

(t) **West Virginia**: The aforementioned practices by Defendants were and are in violation of the West Virginia Antitrust Act, West Virginia Code, Chapter 47, Article 18, §1, *et seq.*;

(u) **Wisconsin**: The aforementioned practices by Defendants were and are in violation of the Wisconsin Antitrust Act, Wisconsin Statutes § 133.01, *et seq*.

137. As a result of Defendants' violations of the aforementioned state laws prohibiting unfair competition, plaintiffs and the Classes are entitled to bring this claim and to recover herein compensatory damages, and where available punitive and special damages, including but not limited to treble damages, reasonable attorneys' fees and costs and other injunctive or declaratory relief as may be available.

## COUNT III

### Unjust Enrichment Under State Law (On Behalf of End Purchaser Internet Music and CD Damages Classes, but Excluding Residents of Florida, North Carolina, and North Dakota)

138. Plaintiffs reallege and incorporate by reference each of the allegations set forth in this complaint. This count is plead in the alternative to the legal claims alleged herein.

139. This Count is alleged against all Defendants, on behalf of the End Purchaser Internet Music and CD Damages Classes but excluding residents of Florida, North Carolina, Montana and North Dakota. Defendants are aware and appreciate that they have been justifiably benefited financially from their unlawful arid inequitable acts alleged in this Complaint. Defendants' financial benefits resulting from their unlawful and inequitable conduct are traceable to overpayments for Internet Music and CDs stemming from Defendants' combination and conspiracy to restrain trade in Internet Music. As a result of

Defendants conspiring, Plaintiffs and class members paid supracompetitive prices for Internet Music and CDs.

140. The Classes purchased their Internet Music and CDs directly from Defendants. The Classes also purchased their Internet Music and CDs indirectly from Defendants through various retailers from whom it would be futile to seek any remedied for the overcharges as they have already reached the Defendants. The Classes have conferred upon Defendants an economic benefit, in the nature of profits resulting from unlawful overcharges, to the economic detriment of plaintiffs and the members of the Classes. Plaintiffs were unaware of the combination and conspiracy and did not knowingly and willingly bestow this benefit on Defendants.

141. The economic benefit of overcharges and unlawful profits sought by and derived by Defendants through charging supracompetitive and artificially inflated prices for Internet Music and CDs is a direct and proximate result of Defendants' unlawful practices.

142. The financial benefits derived by Defendants by reason of their unlawful conduct rightfully belong to plaintiffs and the Classes, as they have paid anticompetitive prices during the Class Period, inuring to the benefit of Defendants.

143. It would be inequitable for the Defendants to be permitted to retain any of the overcharges for Internet Music and CDs derived from Defendants' unfair and unconscionable methods, acts and trade practices alleged in this Complaint.

144. Defendants should be compelled to disgorge into a common fund for the benefit of plaintiffs and

the Classes all unlawful or inequitable proceeds received by them.

145. A constructive trust should be imposed upon all sums unlawfully or inequitably received by Defendants traceable to plaintiffs and the Classes from which plaintiffs and the other Class members may make claims for restitution.

**PRAYER FOR RELIEF**

WHEREFORE, plaintiffs pray that the Court declare, adjudge and decree the following:

A. That this action may be maintained as a class action pursuant to Rule 23(b)(2) of the Federal Rules of Civil Procedure with respect to plaintiffs' claims for declaratory, equitable and injunctive relief, and Rule 23(b)(3) of the Federal Rules of Civil Procedure with respect to the claims for damages and other monetary relief, and declaring plaintiffs as representatives of the Classes and their counsel as counsel for the Classes;

B. That the conduct alleged herein constitutes an unlawful contract, combination or conspiracy to restrain trade and fix and maintain prices in violation of §1 of the Sherman Act, of the state antitrust and unfair deceptive acts and practices statutes set forth herein, and the common law of unjust enrichment;

C. That plaintiffs and the Classes are entitled to any additional damages, penalties and other monetary relief provided by applicable law, including treble damages where allowed by federal or state law;

D. That Defendants disgorge money illegally obtained from the Classes as a result of their unlaw-

ful activities and that members of the Classes are entitled to restitution;

E. That plaintiffs and each member of the Classes are entitled to the amounts by which the Defendants have been unjustly enriched;

F. That Defendants are enjoined from continuing the illegal activities alleged herein;

G. That plaintiffs and the Classes recover their costs of suit, including reasonable attorneys' fees and expenses as provided by law; and

H. That plaintiffs and the Classes are granted such other, further, and different relief as the nature of the case may require or as maybe determined to be just, equitable, and proper by this Court.

**JURY DEMAND**

146. Plaintiffs respectfully demand a trial by jury on all issues so triable.

Dated:
June 13, 2007

LERACH COUGHLIN STOIA
GELLER RUDMAN & ROBBINS
LLP
JOHN J. STOIA, JR. (JS-7507)
CHRISTOPHER M. BURKE (CB-4062)

655 West Broadway, Suite 1900
San Diego, CA 92101
Telephone: 619/231-1058
619/231-7423 (fax)

LOVELL STEWART HALEBIAN
LLP
CHRISTOPHER LOVELL (CL-2595)
CRAIG M. ESSENMACHER
IMTIAZ A. SIDDIQUI (IS-4090)

/s/
CHRISTOPHER LOVELL

500 Fifth Avenue, Suite 5800
New York, NY 10110
Telephone: 212/608-1900
212/719-4677 (fax)

Interim Co-Lead Counsel

BERGER & MONTAGUE, P.C.
EDWARD W. MILLSTEIN
MERRILL G. DAVIDOFF
1622 Locust Street
Philadelphia, PA 19103
Telephone: 215/875-3000
215/875-4604 (fax)

PEARSON SIMON SOTER WARSHAW PENNY LLP
BRUCE L. SIMON
44 Montgomery Street, Suite 1200
San Francisco, CA 94104
Telephone: 415/433-9000
415/433-9008 (fax)

FINKELSTEIN THOMPSON LLP
TRACY D. REZVANI
1050 30th Street, N.W.
Washington, DC 20007
Telephone: 202/337-8000
202/337-8090 (fax)

HULETT HARPER STEWART LLP
BLAKE M. HARPER
DENNIS STEWART
BRIDGET F. GRAMME
550 West C Street, Suite 1600
San Diego, CA 92101
Telephone: 619/338-1133

WHATLEY DRAKE & KALLAS, LLC
JOE R. WHATLEY, JR.
2001 Park Place North, Suite 1000
Birmingham, AL 35203
Telephone: 205/328-9576
205/328-9669 (fax)

Steering Committee

AUDET & PARTNERS, LLP
MICHAEL McSHANE
JOSHUA C. EZRIN
221 Main Street, Suite 1460
San Francisco, CA 94105
Telephone: 415/568-2555
415/568-2556 (fax)

BONNETT, FAIRBOURN, FRIEDMAN & BALINT, P.C.

FRANCIS J. BALINT, JR.
WENDY I. HARRISON
2901 N. Central Avenue, Suite 1000
Phoenix, AZ 85012
Telephone: 602/274-1100
602/274-1199 (fax)

FARUQI & FARUQI, LLP
DAVID H. LEVENTHAL
369 Lexington Avenue, 10th Floor
New York, NY 10017-6531
Telephone: 212/983-9330
212/983-9331 (fax)

FINKELSTEIN & KRINSK LLP
MARK L. KNUTSON
501 West Broadway, Suite 1250
San Diego, CA 92101
Telephone: 619/238-1333
619/238-5425 (fax)

GARDY & NOTTS, LLP
MARK C. GARDY
440 Sylvan Avenue, Suite 110
Englewood Cliffs, NJ 07632
Telephone: 201/567-7377
201/567-7337 (fax)

DAVID PASTOR
DANIEL D'ANGELO
GILMAN AND PASTOR, LLP
225 Franklin Street, 16th Floor
Boston, MA 02110
Telephone: 617/742-9700
617/742-9701 (fax)

GIRARD GIBBS LLP
DANIEL C. GIRARD
ELIZABETH C. PRITZKER
SHERI L. KELLY
601 California Street, Suite 1400
San Francisco, CA 94108
Telephone: 415/981-4800
415/981-4846 (fax)

GLANCY BINKOW & GOLDBERG LLP
SUSAN G. KUPFER
SYLVIE K. KERN
455 Market Street, Suite 1810
San Francisco, CA 94105
Telephone: 4151972-8160
415/972-8166 (fax)

GLANCY BINKOW & GOLDBERG LLP
LIONEL Z. GLANCY
PETER A. BINKOW
MICHAEL GOLDBERG
1801 Avenue of the Stars, Suite 311
Los Angeles, CA 90067
Telephone: 310/201-9150
310/201-9160 (fax)

GROSS & BELSKY LLP
ADAM C. BELSKY
MONIQUE ALONSO

TERRY GROSS
180 Montgomery Street,
Suite 2200
San Francisco, CA 94104
Telephone: 415/544-0200
415/544-0201 (fax)

GUSTAFSON GLUEK PLLC
DANIEL E. GUSTAFSON
DANIEL C. HEDLUND
650 Northstar East
608 Second Avenue South
Minneapolis, MN 55402
Telephone: 612/333-8844
612/339-6622 (fax)

LAW OFFICES OF ALEXANDER M. SCHACK
ALEXANDER M. SCHACK
16870 West Bernardo Drive,
Suite 400
San Diego, CA 92127
Telephone: 858/485-6535
858/485-0608 (fax)

LAW OFFICES OF BRIAN BARRY
BRIAN BARRY
1801 Avenue of the Stars, Suite 307
Los Angeles, CA 90067
Telephone: 310/788-0831
310/788-0841 (fax)

LAW OFFICES OF RANDY R. RENICK
RANDY R. RENICK

JOSH PIOVIA-SCOTT
128 North Fair Oaks Avenue,
Suite 204
Pasadena, CA-91103
Telephone: 626/585-9608
626/577-7079 (fax)

LOCKRIDGE GRINDAL NAUEN
P.L.L.P.
RICHARD A. LOCKRIDGE
R. REID LEBEAU
W. JOSEPH BRUCKNER
100 Washington Avenue South,
Suite 2200
Minneapolis, MN 55401
Telephone: 612/339-6900
612/339-0981 (fax)

MAGER & GOLDSTEIN LLP
JAYNE ARNOLD GOLDSTEIN
1640 Town Center Circle, Suite 216
Weston, FL 33326
Telephone: 954/515-0123
954/515-0124 (fax)

MURRAY & HOWARD, LLP
GILMUR R. MURRAY
DEREK G. HOWARD
SCOTT YUNDT
436 14th Street, Suite 1413
Oakland, CA 94612
Telephone: 510/444-2660
5101444-2522 (fax)

PASKOWITZ & ASSOCIATES

LAURENCE D. PASKOWITZ
60 East 42nd Street, 46th Floor
New York, NY 10165
Telephone: 212/685-0969
212/685-2306 (fax)

REINHARDT WENDORF &
BLANCHFIELD
GARRETT D. BLANCHFIELD, JR.
BRANT D. PENNEY
E-1250 First National Bank Bldg.
332 Minnesota Street
St. Paul, MN 55101
Telephone: 651/287-2100
6511287-2103 (fax)

ROBBINS UMEDA & FINK, LLP
BRIAN S. ROBBINS
610 West Ash Street, Suite. 1800
San Diego, CA 92101
Telephone: 619/525-3990
619/525-3991 (fax)

ROSS DIXON & BELL, L.L.P.
JASON S. HARTLEY
550 West B Street, Suite 400
San Diego, CA 92101
Telephone: 619/235-4040
619/231-8796 (fax)

ROY JACOBS & ASSOCIATES
ROY L. JACOBS
60 East 42nd Street, 46th Floor

New York, NY 10165
Telephone: 212/867-1156
212/504-8343 (fax)

SAVERI & SAVERI, INC.
GUIDO SAVERI
RICHARD A. SAVERI
CADIO ZIRPOLI
111 Pine Street, Suite 1700
San Francisco, CA 94111-3600
Telephone: 415/217-6810
415/217-6813 (fax)

SHALOV STONE BONNER &
ROCCO LLP
RALPH M. STONE
485 Seventh Avenue, Suite 1000
New York, NY 10018
Telephone: 212/239-4340
212/239-4310 (fax)

STEYER LOWENTHAL BOOD-
ROOKAS ALVAREZ & SMITH LLP
ALLAN STEYER
BRYAN MATTHEW KREFT
D. SCOTT MACRAE
One California Street, 3rd Floor
San Francisco, CA 94111
Telephone: 415/421-3400
415/421-2234 (fax)

THE GARCIA LAW FIRM
STEPHEN M. GARCIA
DAVID M. MEDBY
SARINA M. HINSON

One World Trade Center, Suite 1950
Long Beach, CA 90831
Telephone: 562/216-5270
562/216-5271 (fax)

THE MOGIN LAW FIRM, P.C.
DANIEL J. MOGIN
CHAD M. MCMANAMY
110 Juniper Street
San Diego, CA 92101-1502
Telephone: 619/687-6611
619/687-6610 (fax)

Attorneys for Plaintiffs

No. 10-263

# In the Supreme Court of the United States

SONY MUSIC ENTERTAINMENT,
FKA SONY BMG MUSIC ENTERTAINMENT, ET AL.,
*Petitioners*,

v.

KEVIN STARR, ET AL.,
*Respondents*.

*On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit*

## BRIEF IN OPPOSITION


JOHN J. STOIA, JR.
BONNY E. SWEENEY
ROBBINS GELLER RUDMAN
& DOWD LLP
655 West Broadway
Suite 1900
San Diego, CA 92101
(619) 231-1058

CHRISTOPHER LOVELL
*Counsel of Record*
GARY S. JACOBSON
LOVELL STEWART HALEBIAN
JACOBSON LLP
61 Broadway
Suite 501
New York, NY 10006
(212) 608-1900
clovell@lshllp.com

*Counsel for Respondents*


November 22, 2010


Becker Gallagher · Cincinnati, OH · Washington, D.C. · 800.890.5001

## QUESTIONS PRESENTED

In their Fed.R.Civ.P. 12(b)(6) motions to dismiss a claim for agreement to fix prices in violation of Section 1 of the Sherman Antitrust Act, Defendants failed to articulate how certain of the alleged facts could be considered independent, self-interested conduct. *E.g.*, (1) the chief executive of one Defendant admitted that the Defendants had formed joint ventures expressly so that "we [the music industry] determine" and control prices; and (2) the chief executive of another Defendant admitted that the Defendants placed their parallel "most favored nations" clauses in "secret side letters" because "there are legal/antitrust reasons why it would be bad idea to have MFN clauses in any, or certainly all, of these agreements."

In rejecting Defendants' factually incomplete arguments, the Court of Appeals for the Second Circuit quoted from and applied this Court's standards for pleading plausible grounds to infer an illegal agreement under Rule 8 of the Federal Rules of Civil Procedure, as recently articulated in *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544 (2007) and in *Ashcroft v. Iqbal,* 129 S.Ct. 1937 (2009), to **fourteen separate facts** which it found were probative of a prior agreement to fix prices. Defendants' arguments for rehearing or rehearing *en banc* were unanimously rejected. Pet.App.30a-31a.

In such motions, Defendants also failed to cite to *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005), and to argue (as they do here) that Fed.R.Civ.P. 8 requires a plaintiff "to allege those facts

in a complaint that the plaintiff will later need to substantiate at summary judgment or prove at trial."

**Question #1.** Where Defendants failed even to try to articulate how their chief executives' inculpatory admissions are consistent with independent action, have Defendants satisfied their burden as movants on a Fed.R.Civ.P. 12(b)(6) motion to dismiss?

**Question #2.** In light of this Court's express rejection in *Twombly* and *Iqbal* of a "probability" standard under Rule 8, did the court of appeals err in concluding that Plaintiffs alleging a conspiracy under Section 1 of the Sherman Act were not required to plead facts which satisfy a probability standard, to-wit, which "tend to rule out even the **'possibility'** that independent self-interested conduct" is an explanation for Defendants' parallel behavior?

**Question #3.** Where Defendants failed to articulate below the sole question presented by the Petition --- whether, under Rule 8, a complaint must allege "sufficient facts that, if proved, plausibly show an entitlement to relief under the substantive legal standard that will govern the claim at summary judgment or trial" --- should this Court follow its usual practice and decline to consider the question in the first instance?

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## BRIEF IN OPPOSITION

## COUNTERSTATEMENT OF THE CASE

In 2008-2009, the United States took unprecedented actions to try to stop the snowball of deleterious effects from too much capitalism and efficiency and not enough law, deterrence, and individual character. *Compare, e.g.*, Richard A. Posner, THE CRISIS OF CAPITALIST DEMOCRACY, (Harvard University Press, 2010) (reliance on corporate self-interest and the market to police wrongdoing, and discouragement of judicial and regulatory deterrence, were mistaken) *with* Richard A. Posner, THE FAILURE OF CAPITALISM, (Harvard University Press 2009) (same).

Seeking to shift the imbalance of efficiency over law further in the wrong direction, the Petitioners-Defendants ("Defendants") moved under Fed.R.Civ.P. 12(b)(6) to have the courts below dismiss price-fixing conspiracy charges against Defendants, and Defendants

> (a) did not deign to mention, much less try to explain, the alleged inculpatory admissions of two of Defendants' chief executives (Pet.App.16a-17a), and
>
> (b) effectively argued for the "probability" standard that was expressly rejected in *Twombly,* 550 U.S. at 556.

Such inculpatory admissions were that Defendants originally combined together to determine and control prices and later each engaged in the highly unusual

behavior of hiding most-favored-nations clauses in side agreements due to antitrust concerns. Second Consolidated Amended Complaint ("complaint" or "C") ¶¶86,95;Pet.App.93a, 95a.

In rejecting Defendants' factually incomplete arguments, the Court of Appeals for the Second Circuit quoted from and applied this Court's standards for pleading plausible grounds to infer an illegal agreement under Rule 8 of the Federal Rules of Civil Procedure, as recently articulated in *Twombly* and in *Iqbal,* to **fourteen separate facts** which it found were probative of a prior agreement to fix prices. Defendants' arguments for rehearing or rehearing *en banc* were unanimously rejected. Pet.App.30a-31a.

Defendants are the four largest music labels. C¶40;Pet.App.79a. Respondents-Plaintiffs ("Plaintiffs") allege that Defendants agreed and conspired to fix prices and other terms for music sold as digital files ("Digital Music"). C¶2;Pet.App.68a. The primary means of delivery of Digital Music are: (1) online via the Internet ("Internet Music"); and (2) compact discs ("CDs"). *Id.* Plaintiffs allege that, by uniformly requiring Plaintiffs and other purchasers of Digital Music to pay identical supracompetitive prices and to agree to identical idiosyncratic and unpopular digital rights management ("DRM") terms of use, Defendants actually sought to discourage the purchase of their Internet Music so as to protect and increase their CD sales. C¶¶66,82,105;Pet.App.85a,90a,97a-98a.

Defendants have a history of alleged antitrust violations.[1]

Consistent with their history of alleged anticompetitive behavior, the chief executive officer of one Defendant explained that the formation of Defendants' "pressplay" Internet Music joint venture was for the purpose of determining and controlling prices. Pet.App.16a.

Consistent with their history of alleged anticompetitive behavior, the chief executive officer of another Defendant decided that his company's "most favored nations" ("MFN") agreement with Defendants' joint venture MusicNet (which assured that each Defendant's core terms would be no less favorable than those of the other Defendants) would be placed in "a secret side letter" because "there are legal/antitrust reasons why it would be a bad idea to have MFN clauses in any, or certainly all, of these agreements." Pet.App.16a-17a.

Consistent with their history of alleged anticompetitive behavior, Defendants in about May 2005 raised wholesale prices from about $0.65 per song to $0.70 per song, "even though earlier that year defendants' costs of providing Internet Music had decreased substantially due to completion of the initial cataloging of all Internet Music and technological

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[1] *E.g., In re Compact Disc Minimum Advertised Price Antitrust Litig.*, 216 F.R.D. 197 (D. Me. 2003) (finally approving settlement); *In re Sony Entm't, Inc.*, No. C-3971, 2000 WL 1257796 (F.T.C. Aug. 30, 2000) (consent decrees against distributor defendants); *In re Compact Disc Litig.*, MDL No. 1216 (C.D.Cal. 1997); *Ottinger v. EMI Music Distrib.*, No. 24865-II (Tenn. Cir. Ct.).

improvements that reduced the cost of digitizing new releases." Pet.App.17a.

In addition to the foregoing, the Second Circuit in its decision below (the "Decision") cited to the following "non-conclusory factual allegations" of the complaint as providing plausible grounds for inferring an illegal agreement:

- Defendants agreed to launch the joint ventures MusicNet and pressplay, both of which charged unreasonably high prices and contained similar DRMs. Pet.App.14a.

- None of the defendants dramatically reduced their prices for Internet Music (as compared to CDs), despite the fact that all defendants experienced dramatic cost reductions in producing Internet Music. *Id.*

- When defendants began to sell Internet Music through entities they did not own or control, they maintained the same unreasonably high prices and DRMs as MusicNet itself. *Id.*

- Defendants used MFNs in their licenses that had the effect of guaranteeing that the licensor who signed the MFN received terms no less favorable than terms offered to other licensors. *Id.*

- According to the executive director of the Digital Music Association, seller-side MFNs such as those alleged here are "inherently price-increasing and anticompetitive." Pet.App.17a.

- Defendants used the MFNs to enforce a wholesale price floor of about 70 cents per song. Pet.App.15a.

- All Defendants refuse to do business with eMusic, the # 2 Internet Music retailer. *Id.*

- In or about May 2005, all defendants raised wholesale prices from about $0.65 per song to $0.70 per song, an increase enforced by MFNs. *Id.*[2]

- Defendants control over 80% of Digital Music sold to end purchasers in the United States. Pet.App.16a.

- An industry commentator noted that "nobody in their right mind" would want to use MusicNet or pressplay, suggesting that some form of agreement among Defendants would have been needed to render the enterprises profitable. *Id.*

- Whereas eMusic charges $0.25 per song, Defendants' wholesale price is about $0.70 per song. Pet.App.17a.

- Defendants' price-fixing is the subject of a pending investigation by the New York State

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[2] The Second Circuit included the allegations in proposed amended ¶ 99 of the complaint, which amendment contained "enough fact to raise a reasonable expectation that discovery will reveal evidence of an illegal agreement," and thus had erroneously been denied by the district court. Pet.App.15a n. 3 (citing *Twombly*, 550 U.S. at 556).

> Attorney General and two separate investigations by the Department of Justice. *Id.*[3]

In sum, the Second Circuit concluded that "[t]he present complaint succeeds where *Twombly*'s failed because the complaint alleges specific facts sufficient to plausibly suggest that the parallel conduct alleged was the result of an agreement among the defendants." Pet.App.14a. The fact-specific Decision raises no issue meriting review by this Court.

**Proceedings Below**

This multidistrict litigation consolidated for pretrial proceedings twenty-eight actions alleging that Defendants had agreed to fix the prices of Digital Music and had engaged in related wrongs. Plaintiffs filed a Second Consolidated Amended Complaint (the "complaint") in the United States District Court for the Southern District of New York on June 13, 2007, alleging that Defendants' agreement violated Section 1 of the Sherman Act as well as the antitrust, trade regulation, consumer protection and common laws of numerous States and the District of Columbia.

On July 30, 2007, Defendants moved, pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure,

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[3] Defendants' factual assertions pertaining to two government investigations, offered herein for their truth, contradict the express allegations of the Complaint and must be disregarded on a Rule 12(b)(6) motion. C¶¶106-15;Pet.App.98a-99a. *See High Fructose Corn Syrup Antitrust Litig.*, 295 F.3d 651, 664 (7th Cir. 2002) (Posner, J.) (fact that DOJ saves its limited resources and leaves enforcement to private bar raises no inference against claim of conspiracy).

for an order dismissing the complaint for failure to state a claim as to which relief may be granted. Defendants argued that the complaint failed adequately to plead an agreement to fix prices under the pleading standards enunciated by *Twombly,* and also raised certain other grounds applicable to the State law claims. Plaintiffs responded on September 13, 2007, arguing that *Twombly* and the Rule 8(a)(2) standards required only plausibility, not probability, and that the complaint satisfied the standard. Defendants replied on October 15, 2007, arguing for the first time that Plaintiffs had not adequately alleged that Defendants' significant parallel price increases for Internet Music in 2005 had occurred at a time when Defendants' costs of providing Internet Music had declined. With the district court's permission, Plaintiffs moved to amend paragraph 99 of the complaint to allege more details in this respect. Defendants opposed the motion.

The district court granted the motions to dismiss, interpreting *Twombly* to require that "factual enhancements" that tend to exclude the possibility of independent action "must appear in a § 1 plaintiff's complaint," Pet.App.42a, and holding that the complaint "does not allege the further facts required by *Twombly* to state a § 1 claim based upon parallel conduct." Pet.App.44a, 55a. The district court held that this also required dismissal of the State claims, Pet.App.55a-66a, and it denied as "futile" Plaintiffs' motion to amend. Pet.App.52a n. 14.

The Second Circuit vacated the judgment. The court set out the standards from *Twombly* and *Iqbal,* quoted extensively from both cases, and applied the "language and reasoning" of those cases to the facts of

the complaint, including the fourteen facts the Second Circuit enumerated above. It concluded that "[t]his complaint does not resemble those our sister circuits have held fail to state a claim under *Twombly*." Pet.App.17a-18a (citations omitted).

## REASONS FOR DENYING THE PETITION

The Petition is a fatally flawed vehicle seeking the improper goal of judicial amendment of Rule 8. By not attempting to articulate a response to the complaint's critical allegations, the Defendants failed their burden under Rule 12(b)(6).

Defendants' assertion that the Second Circuit erred by not imposing a summary judgment plausibility pleading standard is meritless. In holding that Rule 8 of the Federal Rules of Civil Procedure requires an antitrust plaintiff to allege "enough factual matter (taken as true) to suggest that an agreement was made," *Twombly*, 550 U.S. at 556, this Court made clear that: "Asking for plausible grounds to infer an agreement does not impose a probability requirement at the pleading stage; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement. And, of course, a well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and that a recovery is very remote and unlikely." *Id.* (citation and internal quotation marks omitted). The lower courts have uniformly understood and applied the "plausible pleading" standard announced by this Court in *Twombly* and *Iqbal* as not imposing a "probability" requirement.

The Second Circuit correctly quoted, followed and applied this Court's standards to the extensive, detailed facts pleaded in the complaint. In arguing that complaints must allege facts which "tend to exclude" independent action, Defendants seek the same plausibility standard which Defendants' counsel successfully (and correctly) argued in a different case was expressly disclaimed in *Twombly*. Superimposing onto *Twombly* the "*Matsushita* 'tends to exclude' standard for summary judgment," Petition at 17 n. 3,[4] Defendants seek to create precisely the "probability requirement" that *Twombly* rejected.

Finally, by posing a new question seeking an even broader ruling than they sought below, and by citing a securities case which they did not cite below, Defendants have without justification asked this Court to consider the question in the first instance, which the Court should decline to do.

Thus, it is the Petition, not the Decision, which conflicts with *Twombly*.

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[4] *Twombly* described the standard as requiring that on summary judgment, "a § 1 plaintiff's offer of conspiracy evidence must "tend to rule out the possibility that the defendants were acting independently." 550 U.S. at 554 (citing *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 752 (1984)); *see also id.* (citing *Monsanto Co. v. Spray-Rite Service Corp.*, 564 U.S. 752 (1984) ("proof of a § 1 conspiracy must include evidence tending to exclude the possibility of independent action").

## I. DEFENDANTS' FAILURE TO ARTICULATE AN EXPLANATION FOR THEIR CHIEF EXECUTIVES' ADMISSIONS DID NOT SATISFY THEIR BURDEN ON THE MOTIONS TO DISMISS, AND THE DENIAL OF THOSE MOTIONS RAISES NO ISSUE FOR REVIEW

The Second Circuit noted allegations that two of Defendants' chief executives had made admissions suggestive of a prior illegal agreement: that Defendants had formed joint ventures to "determine" and control prices, and that MFN agreements would be kept secret for "legal/antitrust reasons." Pet.App.16a-17a. Defendants never tried to articulate how either of those admissions could be probative of independent self-interested conduct.

Challenges to a complaint for failure to state a claim are ordinarily made, as they have been made here, under Fed.R.Civ.P. 12(b)(6). *See Bell v. Hood*, 327 U.S. 678, 682 (1946). Under Rule 12(b)(6), the moving defendant bears the burden of showing that no claim has been stated. *E.g.*, *Kehr Packages, Inc. v. Fidelcor, Inc.*, 926 F.2d 1406, 1409 (3d Cir.), *cert. denied*, 501 U.S. 1222 (1991); 5B Charles Wright & Arthur Miller, FEDERAL PRACTICE AND PROCEDURE § 1357 (3d ed. 2010 supp.) ("All federal courts are in agreement that the burden is on the moving party to prove that no legally cognizable claim for relief exists."). Rule 12(b)(6) thus provides procedural protections to the plaintiff which "alert him to the legal theory underlying the defendant's challenge, and enable him meaningfully to respond by opposing the motion to dismiss on legal grounds or by clarifying his factual allegations so as to conform with the

requirements of a valid legal cause of action." *Neitzke v. Williams*, 490 U.S. 319, 329-30 (1989).

Defendants made no effort to articulate a response to key allegations of the complaint and thus failed their movants' burden under Rule 12(b)(6). Defendants' failure independently sustains the Decision, and the Petition presents no issue for this Court's review.

## II. THE SECOND CIRCUIT'S CORRECT APPLICATION OF THIS COURT'S RULE 8 DECISIONS TO THE ROBUST FACTUAL ALLEGATIONS OF THE COMPLAINT PRESENTS NO ISSUE FOR REVIEW

No court has adopted Defendants' argument that *Twombly* and *Iqbal* changed Rule 8(a)(2)'s "short and plain statement of the claim showing that the pleader is entitled to relief" to require, on a Rule 12(b)(6) motion, that the complaint allege facts sufficient to "satisfy the same substantive legal standard that applies at summary judgment or trial." Petition at 15. Pasting together isolated words and phrases from *Twombly, Iqbal* and *Dura*, both Defendants' newly proposed standard and their proposed "tends to exclude" standard amount to the very "probability" standard disclaimed in *Twombly* and *Iqbal*. The court so held in *Flying J, Inc. v. TA Operating Corp.*, No. 1:06-CV-30-TC, 2007 WL 4165749 at *2 (D.Utah Nov. 20, 2007), denying defendants' Rule 12(c) motion and rejecting defendants' argument for a "tends to exclude" standard as "contrary to the language of *Twombly*" and

that case's express disclaimer that it was imposing a "probability" standard.[5]

The Second Circuit painstakingly quoted and correctly applied the *Twombly* and *Iqbal* standards to the very extensive and robust fact allegations of the complaint --- including fact allegations which negated any lawful explanation for Defendants' conduct and which Defendants, in three sets of briefs below, conspicuously failed to mention, let alone try to explain. The Petition presents no issue meriting this Court's review.

### A. The Second Circuit Correctly Applied This Court's Rule 8 Standards to the Robust Allegations of the Complaint

Unable to avoid the complaint's non-conclusory fact allegations[6] of conduct placed in a "context that raises a suggestion of a preceding agreement," *Twombly*, 550 U.S. at 557, Defendants argued that *Twombly* required a Section 1 plaintiff to allege facts that "tend[] to exclude independent self-interested conduct as an

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[5] Defendants' counsel in this case successfully argued in *Flying J* that *Twombly* **did not adopt** a standard requiring plaintiffs to allege "additional facts that tend to exclude independent self-interested conduct as an explanation for defendants' parallel behavior." Plaintiffs' Memorandum in Opposition to TA's and Pilot Defendants' Motion for Judgment on the Pleadings at 7-9, submitted in *Flying J, Inc. v. TA Operating Corp.*, No. 1:06-CV-30-TC, Doc. No. 157 (D.Utah, Aug. 20, 2007).

[6] The Second Circuit did not accept as true those of the complaint's allegations that it considered were "no more than conclusions." Pet.App.3a n. 1 (citing *Iqbal*, 129 S.Ct. at 1949-50); *see also id.* at 6a n.2 (rejecting allegation as conclusory).

explanation for defendants' parallel behavior." Pet.App.18a. The Second Circuit properly rejected the argument.

> This is incorrect. Although the *Twombly* court acknowledged that for purposes of summary judgment a plaintiff must present evidence that tends to exclude the possibility of independent action, 550 U.S. at 554, 127 S.Ct. 1955, and that the district court below had held that plaintiffs must allege additional facts that tended to exclude independent self-interested conduct, *id.* at 552, 127 S.Ct. 1955, it specifically held that, to survive a motion to dismiss, plaintiffs need only [allege] 'enough factual matter (taken as true) to suggest that an agreement was made,' *id.* at 556, 127 S.Ct. 1955; *see also* 2 Areeda & Hovenkamp [ANTITRUST LAW] § 307d1 (3d ed. 2007) ('[T]he Supreme Court did ***not*** hold that the same standard applies to a complaint and a discovery record.... The "plausibly suggesting" threshold for a conspiracy complaint remains considerably less than the "tends to rule out the possibility" standard for summary judgment.').

*Id.* (emphasis in original).[7]

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[7] Defendants' counsel in this case has written that the existence of scholarly opinion, most particularly from the Areeda-Hovenkamp treatise, "appears to be one of the most important factors in the Court's decision whether to grant certiorari in an antitrust case." Thomas G. Hungar and Ryan G. Koopmans, *Appellate Advocacy in Antitrust Cases: Lessons from the Supreme Court*, ANTITRUST (Vol. 23, No. 2, Spring 2009) at 54-55, available at http://www.gibsondunn.com/publications/Documents/Hungar-AppellateAdvocacyInAntitrustCases.pdf.

Contrary to Defendants' unsupported argument that the court adopted "an amorphous consideration of 'context' unmoored to the correct legal standard," Petition at 22, the Second Circuit correctly applied *Twombly*'s requirement for "context."

> [A]n allegation of parallel conduct coupled with only a bare assertion of conspiracy is not sufficient to state a Section 1 claim. [*Twombly*, 550 U.S. at 556]. Instead, allegations of parallel conduct 'must be placed in a context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action.' *Id.* at 557, 127 S.Ct. 1955.

*Id.* at 12a. The Second Circuit scrupulously followed "the language and reasoning" of *Twombly* in applying those standards to the facts alleged. *Id.* at 14a. The court correctly found that particular allegations place the parallel conduct in the required context. *Id.* at 12a, quoting *Twombly*, 550 U.S. at 557. In consideration of Defendants' failure to offer any "obvious alternative explanation" in response to Plaintiff's allegations, *see* Point II.E. *infra*, the court also correctly concluded that "in this case plaintiffs have alleged behavior that would plausibly contravene each defendant's self-interest 'in the absence of similar behavior by rivals.'" Pet.App.24a (citations omitted).

### B. The Second Circuit Correctly Determined That *Twombly* Did Not Impose a Summary Judgment Standard on Motions to Dismiss

Defendants' insistence that *Twombly* applied the summary judgment standard in dismissing an

antitrust complaint under Rule 8, Petition at 14, denies the plain language of the decision. *Twombly* required not that plaintiffs allege facts which "tended to exclude" independent conduct, but rather that they allege "enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement." 550 U.S. at 556. *Twombly* endorsed Rule 8's "general standards," *id.*,[8] including accepting the well-pleaded allegations as true (whether or not they are believed) and drawing all reasonable inferences from such allegations in favor of plaintiffs. Although it did not require "particularity," *Twombly* required pleading "more than labels and conclusions" in support of grounds that "raise a right to relief above the speculative level." *Id.* at 555-56.

*Twombly*'s new "gloss" on the well-settled standards of Rule 8(a)(2) did not include any requirement that a plaintiff plead facts tending to negate the possibility that defendants had acted from their independent self-interest rather than from agreement to divide markets in violation of Section 1 of the Sherman Act:

> In applying these general standards to a § 1 claim, we hold that stating such a claim requires a complaint with enough factual matter (taken as true) to suggest that an agreement was made. **Asking for plausible**

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[8] For example, *Twombly* did not disturb Rule 8(a)(2)'s requirement that a complaint provide only "'a short and plain statement of the claim showing that the pleader is entitled to relief.' Specific facts are not necessary; the statement need only 'give the defendant fair notice of what the ... claim is and the grounds upon which it rests.' *Erickson v. Pardus*, 551 U.S. 89, 93 (2007) (collecting cases).

> **grounds to infer an agreement does not impose a probability requirement at the pleading stage; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement.** And, of course, a well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and 'that a recovery is very remote and unlikely.'

*Id.* at 556 (emphasis supplied) (footnote omitted), quoting *Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974). A plaintiff's allegations need only raise a plausible, not probable, inference of agreement in order to permit the case to go forward. *Twombly* also confirmed that Rule 8(a)(2) requires no heightened degree of pleading particularity, and that the heightened standard of Federal Rule 9(b) does not apply in determining whether a Section 1 claim has been stated. *Id.* at 569 n. 14 (broadening the scope of Rule 9 "can only be accomplished 'by the process of amending the Federal Rules, and not by judicial interpretation'"). Defendants' argument that *Twombly* raised the motion-to-dismiss standard to that for submitting evidence on summary judgment thus finds no support in *Twombly*.

Defendants misconstrue this Court's discussion of the *Twombly* district judge's use of the term "plus factors" to augment bare allegations of parallel conduct:

> The Court also noted that Judge Lynch, who authored the district court opinion in *Twombly*, 'understood that allegations of parallel business

> conduct, taken alone, do not state a claim under § 1; plaintiffs must allege additional facts that "ten[d] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior.'" *Id.* at 552 (citation omitted).

Petition at 14. The citation omitted by Defendants was to the district court's decision in *Twombly v. Bell Atlantic Corp.*, 313 F.Supp.2d 174, 179 (S.D.N.Y. 2003), where the district court actually said:

> **In the summary judgment context,** the Second Circuit requires plaintiffs to **present evidence** suggesting that the defendants' parallel conduct has resulted from an agreement rather than 'merely from independent ... conduct by firms acting in their own self-interests.' *Kramer v. Pollock-Krasner Found.*, 890 F.Supp. 250, 255 (S.D.N.Y.1995) (citing *Apex Oil Co. v. DiMauro*, 822 F.2d 246, 254 (2d Cir.1987)). Plaintiffs may satisfy this standard by **establishing at least one 'plus factor' that tends to exclude independent self-interested conduct as an explanation for defendants' parallel behavior**. The plus factors include **evidence** that the parallel behavior would have been against individual defendants' economic interests absent an agreement, or that defendants possessed a strong common motive to conspire. *Apex Oil*, 822 F.2d at 253-54.

313 F.Supp.2d at 179 (emphasis supplied). By his express qualifier to "the summary judgment context," and by the citation to the *Apex Oil* summary judgment decision, it is clear that then-District Judge Lynch

"understood" that the "tends to exclude" standard referred to evidence submitted on motions for summary judgment. *See also id.* at 179-80 (separate and distinct from summary judgment, district courts in the Second Circuit have required antitrust plaintiffs asserting parallel conduct conspiracies to "allege plus factors" in order to withstand motions to dismiss; where plaintiffs "allege parallel action that **could be** the result of a conspiracy . . . plaintiffs are entitled to [go forward and] explore in discovery. . . .") (emphasis supplied).

This Court's citation to the district court's *Twombly* decision does not suggest a heightened standard requiring the pleading of evidentiary "plus factors." Indeed, that term is virtually absent from *Twombly*. *Twombly* holds that a Section 1 complaint alleging parallel conduct must also contain "additional facts," 550 U.S. at 552, 570, or some "further circumstance," *id.* at 557, in order to provide plausible grounds for inferring the agreement which makes the parallel conduct unlawful. Because bare allegations of parallel conduct do not without more suggest conspiracy, such "additional facts" are necessary at the pleading stage in order adequately to notify the defendant of the nature of the claim. *Id.* Thus, *Twombly* stated that the district court had "correctly understood" that requiring that "further circumstances" be alleged did not run counter to the rule, reemphasized in *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506 (2002), that imposing a higher pleading standard under Rule 8 "was contrary to the Federal Rules' structure of liberal

pleading requirements." 550 U.S. at 570, citing *Twombly*, 313 F.Supp.2d, at 181.[9]

Defendants fail to distinguish *Swierkiewicz*. The fact that *Swierkiewicz* predated *Twombly* is irrelevant, since *Twombly* expressly reaffirmed *Swierkiewicz*. 550 U.S. at 570. Defendants' suggestion that *Swierkiewicz*'s holding is limited to plaintiffs relying on direct evidence is refuted by the plain language of the decision, which rejects different pleading requirements "at the time of his complaint" for plaintiffs who might ultimately use direct evidence and plaintiffs who might ultimately use circumstantial evidence.

> Under the Second Circuit's heightened pleading standard, a plaintiff without direct evidence of discrimination at the time of his complaint must plead a prima facie case of discrimination, even though discovery might uncover such direct evidence. It thus seems incongruous to require a plaintiff, in order to survive a motion to dismiss, to plead more facts than he may ultimately need to prove to succeed on the

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[9] Contrary to Defendants' argument, the *Twombly* dissent, while apparently disagreeing with the majority's assessment of the plausibility of the complaint before the court, does not state that the majority applied a summary judgment standard to the complaint. *Compare Twombly*, 550 U.S. at 586 (Stevens, J., dissenting) ("I have my doubts about the majority's assessment of the plausibility of this alleged conspiracy.") *with Iqbal*, 129 S.Ct. at 1960 (Souter, J., dissenting) ("Iqbal's complaint therefore contains 'enough facts to state a claim for relief that is plausible on its face.'") (citation omitted).

> merits if direct evidence of discrimination is discovered.

534 U.S. at 511-12.

In sum, *Twombly*'s requirement that a Section 1 plaintiff allege facts which provide fair notice of his claim and plausible grounds of his entitlement to relief, does not impose a requirement that a plaintiff plead evidence which tends to exclude (or eliminates the possibility of) independent self-interested conduct as an explanation for defendants' parallel behavior.

### C. The Second Circuit Correctly Determined That *Iqbal* Did Not Impose a Summary Judgment Standard on Motions to Dismiss

*Iqbal*, a civil rights case, made explicit that application of the *Twombly* "plausible pleading" standard was not limited to antitrust complaints. 129 S.Ct. at 1953. Contrary to Defendants' arguments, however, *Iqbal* does not require a summary judgment pleading standard. Plaintiffs in *Iqbal* challenged the constitutionality of their pretrial confinement after they had been classified as persons of "high interest" because of their suspected links to the September 11 attacks. They asserted that the challenged detention policies purposefully discriminated against Arab Muslim defendants on prohibited grounds. Although the well-pleaded allegations of the complaint are deemed to be true on a Rule 12(b)(6) motion, the Court deemed plaintiffs' allegations that the Attorney General and the director of the FBI "willfully and maliciously agreed" to subject plaintiffs to harsh conditions of confinement conclusory, and therefore not entitled to the presumption of truth. Absent those

allegations, the majority held that plaintiffs had not stated a plausible claim. *Iqbal* thus explained *Twombly* as holding that "[a] claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged....Determining whether a complaint states a claim for relief will ... be a context-specific task that requires the reviewing court to draw on its judicial experience and common sense." *Iqbal*, 129 S. Ct. at 1949-50.

Defendants misstate *Iqbal*'s description of *Twombly*'s holding to be as follows: "Because the plaintiffs' allegations of parallel conduct failed to exclude 'lawful, unchoreographed free-market behavior,' the complaint 'did not plausibly suggest an unlawful agreement.'" Petition at 14, citing *Iqbal*, 129 S.Ct. at 1950 (citing *Twombly*, 550 U.S. at 567, 570). *Iqbal* neither required, nor construed *Twombly* to require, that a complaint "exclude" anything. Rather, *Iqbal* described the parallel conduct allegations in *Twombly* as "more likely explained by" lawful behavior under the long-standing business environment in the telecommunications industry. *Iqbal*, 129 S.Ct. at 1950. *Iqbal*'s characterization of the *Twombly* defendants' conduct as "more likely explained by" lawful behavior was, again, not announcing a "probability" requirement. Rather, the Court was making a common sense observation that the *Twombly* defendants, previously prohibited from each others' markets, could not by their **parallel inaction** in a changed regulatory environment be plausibly inferred to be conspiring. *Twombly*, 550 U.S. at 566. There thus existed "an obvious alternative explanation" for defendants' inaction. *Id.* at 567.

Defendants seize upon the snippet "[i]t follows," constructing a facially flawed argument that "it follows" from *Iqbal*'s citation to summary judgment decisions that it was applying the summary judgment evidentiary standard to the complaint's allegations on a motion to dismiss. Petition at 15, quoting 129 S.Ct. at 1948-49. *Iqbal*, however, also made clear that "[t]he plausibility standard is not akin to a 'probability requirement,' but it asks for more than a sheer possibility that a defendant has acted unlawfully." 129 S.Ct. at 1949, citing *Twombly*, 550 U.S. at 556. Thus, as the parallel conduct alleged in *Twombly* remained, without more, in "neutral territory," 550 U.S. at 557, so the conduct alleged in *Iqbal* did not provide due notice of the claim and its grounds under Rule 8, unless facts were alleged "plausibly showing that petitioners purposefully adopted a policy of classifying post-September-11 detainees as 'of high interest' because of their race, religion, or national origin." 129 S.Ct. at 1952. It plainly does not "follow" that the Court was requiring satisfaction of the summary judgment evidentiary standard by requiring plaintiff to plead "more than a sheer possibility that a defendant has acted unlawfully." *Id.* at 1949.

### D. Should the Court Consider Defendants' New-Found Reliance on a Securities Fraud Case, That Case Did Not Impose a Summary Judgment Standard on Motions to Dismiss

In light of Defendants' failure to cite or present any argument regarding *Dura Pharmaceuticals* to any court below, this Court should follow its usual practice and decline to consider it now. *See* Point III *infra*. Should the Court consider *Dura*, that case provides no

support for the summary judgment pleading standard Defendants seek here.

*Dura*, a case brought under the elevated pleading standards of the Private Securities Litigation Reform Act, held that plaintiffs' allegation of share purchases at an inflated price insufficiently alleged proximate causation. *Dura* did not impose a summary judgment standard at the pleading stage, or "any special further requirement in respect to the pleading of proximate causation or economic loss" under Rule 8. *Dura*, 544 U.S. at 346. Rather, the Court considered the "pure logic" of share transactions to be that any loss occurs not at the time of the inflated-priced purchase but at the lower-priced sale, which lower price may reflect, in whole or in part, facts or conditions not suggestive of wrongdoing. *Id.* at 342-43. Thus, a securities complaint does not provide defendants with "fair notice of what the plaintiff's claim is and the grounds upon which it rests," *id.* at 346 (citation omitted), if it fails to plead "some indication of the loss and the causal connection that the plaintiff has in mind." *Id.* at 347 (citing *Swierkiewicz*, 534 U.S. at 513-15). This again is hardly "a substantive legal standard that will govern the claim at summary judgment or trial."

### E. Although Defendants Complain that the Second Circuit Failed to Consider "Obvious Alternative Explanations" for Their Conduct, Defendants Never Offered Such Explanations

Defendants argue that the Second Circuit erroneously failed to test the plausibility of the complaint's allegations against "obvious alternative explanations" for defendants' conduct. Petition at 19-

22. But the Second Circuit was well aware of *Twombly*'s requirements and concluded that "in this case plaintiffs have alleged behavior that would plausibly contravene each defendant's self-interest 'in the absence of similar behavior by rivals.'" Pet.App.24a (citations omitted). Defendants' real grievance is not that the Second Circuit failed to consider obvious alternative explanations; it is that the court disagreed that Defendants had offered any. Such disagreement with factual findings does not provide a good ground for granting the writ of certiorari. *See* Rule 10, Rules of the Supreme Court of the United States.

Defendants have never explained why their interest in combating illegal downloading of music on the Internet, a subject which does not appear in the complaint,[10] provided an "obvious alternative explanation" for their conduct. Considering such alternatives within the context of the complaint requires a court "to draw on its judicial experience and common sense." *Iqbal*, 129 S.Ct. at 1950. In order for an explanation to be an "obvious alternative," it must at a minimum comport with common sense.

Defendants uniformly imposed supracompetitive prices and onerous DRM terms, by which consumers were restricted in their downloading, copying and use of Defendants' Internet Music and, after a period, could actually lose access to those downloads. C¶¶74-77;Pet.App.87a-89a. The common sense effect of

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[10] The district court thus had to reach outside the complaint to consider "an environment of widespread unauthorized downloading of Internet Music." Pet.App.44a-45a & nn. 9, 10.

Defendants' conduct was not to combat illegal downloading, but to drive customers away from Defendants' Internet Music. Defendants have not explained how their alleged conduct made economic or common sense as a response to "Internet piracy." C¶¶75-82;Pet.App.87a-90a. Rather, the idiosyncratic and unpopular terms uniformly imposed by Defendants made economic sense as creating an incentive for consumers to refrain from purchasing Defendants' Internet Music and instead to purchase Defendants' Digital Music on CDs, a more profitable medium. C¶¶66,82,105;Pet.App.85a,90a,97a-98a.

Indeed, the admission by one of Defendants' chief executives that the joint ventures were formed to control prices demolishes any obvious alternative explanation, at least for the activities of the MusicNet and pressplay joint ventures. Pet.App.16a. Another chief executive's direction that his company's MFN agreements with the joint ventures be put in "secret side letters" raises a plausible inference that Defendants knew of antitrust concerns regarding their entry into seller-side "most favored nations" agreements, which one neutral observer called "inherently price-increasing and anticompetitive." Pet.App.16a-17a. Defendants have never offered an explanation which would explain why they even needed joint ventures to effectuate their agreement.

The Second Circuit followed this Court's standards in determining that the inferences to be drawn from Defendants' alleged conduct was that it "plausibly contravene[d]" each Defendant's self-interest in the absence of similar behavior by rivals. Pet.App.24a. The court drew this inference not, as Defendants assert, "based on the opinion of a single industry

commentator," Petition at 21-22, 25, but after a careful review of all Defendants' alleged admissions and conduct which made Defendants' own Internet Music business unpopular. Rather than intended to address illegal downloading, Defendants' conduct was, as the Second Circuit correctly concluded, plausibly suggestive of a prior agreement to impose non-competitive terms and conditions on Internet Music, which each Defendant could not have accomplished separately, to benefit their more lucrative CD business. Pet.App.24a.

## III. BECAUSE DEFENDANTS FAILED TO RAISE OR LITIGATE BELOW THE SOLE QUESTION THEY PRESENT HERE, THE COURT SHOULD FOLLOW ITS USUAL PRACTICE AND DECLINE TO CONSIDER IT

Having failed to carry their burden below, Defendants now present a single question, which they have never previously raised: "whether the court of appeals erred in holding that a complaint can state a claim without alleging sufficient facts that, if proved, plausibly show an entitlement to relief under the substantive legal standard that will govern the claim at summary judgment or trial." Defendants offer as their first authority *Dura Pharmaceuticals,* a case they never cited below. Although *Dura* does not support any argument Defendants make here (*see* Point II.D. *supra*), this Court should follow its usual practice and decline to decide questions not raised or litigated in the first instance in the lower courts. *See Springfield v. Kibbe*, 480 U.S. 257, 258 (1987); *F.T.C. v. Grolier, Inc.*, 462 U.S. 19, 23 n. 6 (1983).

Defendants' new question misstates the Decision, which rejected the argument Defendants had actually made: that *Twombly* requires a plaintiff to allege facts that "tend[] to exclude independent self-interested conduct as an explanation for defendants' parallel behavior." Pet.App.18a. The Second Circuit held (and the leading commentators have agreed) that *Twombly*'s requirement that a plaintiff allege "enough factual matter (taken as true) to suggest that an agreement was made" is a lesser standard than requiring summary judgment evidence that "tends to exclude" independent conduct. *Id.* (citing *Twombly*, 550 U.S. at 556 and 2 Areeda & Hovenkamp § 307d1 (3d ed. 2007); *see* Point II.A. *supra*.

Defendants' new question goes even further to ask whether, at the time of the complaint, a plaintiff must under *Twombly* not only allege facts which "tend to exclude" the possibility that defendants acted independently, but allege all the facts he will need to prove at trial on the merits. No court has so held, and certainly Defendants have cited no authority which would support such a pleading requirement. Defendants have offered no excuse for their failure to allow consideration of this question by the court of appeals, and this Court should decline to consider it.

## IV. THE SECOND CIRCUIT'S DECISION DOES NOT CONFLICT WITH THE DECISION OF ANY OTHER CIRCUIT COURT

Defendants have not demonstrated that the Decision conflicts with that of any circuit court. Indeed, Defendants have not cited to any court holding that Rule 8 "require[s] a plaintiff to allege those facts

in a complaint that the plaintiff will later need to substantiate at summary judgment or prove at trial." Petition at 12. No court has so held.

*Tam Travel*

Defendants assert that the Sixth Circuit's decision in *Tam Travel, Inc. v. Delta Airlines, Inc.*, 583 F.3d 896 (6th Cir. 2009), which alleged an antitrust conspiracy of airlines to reduce, cap and eliminate commission payments to travel agents, conflicts with the Decision. But, as Defendants correctly state, *Tam Travel* did not hold that a complaint must be evaluated under the "tends to exclude" standard. Rather, as Defendants acknowledge, the Sixth Circuit said only that the *Matsushita* "tends to exclude" standard can "illuminate[] the plausibility" of antitrust conspiracy allegations. Petition at 23. The Sixth Circuit's "illuminate" observation appears in a discussion of a summary judgment decision and is accompanied by a reminder that "[h]ere, our review is constrained by Fed.R.Civ.P. 12(b)(6)." 583 F.3d at 907 n. 7. *Tam Travel* thus did not endorse a standard of "tending to exclude 'reasonable, alternative explanations'" in dismissing the complaint. Petition at 23. Rather, the Sixth Circuit actually held as follows:

> We therefore hold that plaintiffs have failed to allege sufficient facts plausibly suggesting (not merely consistent with) an agreement in violation of § 1 of the Sherman Act because defendants' conduct 'was not only compatible with, but indeed was more likely explained by, lawful, unchoreographed free-market behavior.'

*Id.* at 908 (quoting *Iqbal*, 129 S.Ct. at 1950). The actual holding thus used language taken directly from *Iqbal* and *Twombly*, rather than the "tending to exclude" formulation for summary judgment, and raises no conflict with the Decision.

Nor is *Tam Travel*'s use of *Iqbal*'s description of defendants' conduct as "more likely explained by" independent behavior an adoption of the probability/summary judgment standard expressly disclaimed in *Twombly and Iqbal.*[11] As used in *Iqbal*, the phrase again refers to Defendants' conduct being in "neutral territory," according to evidence available by reason of the fact that *Tam Travel* was brought by plaintiffs who had opted out of the putative class in *Hall v. United Air Lines, Inc.*, 296 F.Supp.2d 652 (E.D.N.C. 2003). *Tam Travel*, 583 F.3d at 900 n. 3. The Sixth Circuit noted that defendants had won summary judgment in *Hall*, after the district court

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[11] The Sixth Circuit described its standard of review as

> recogniz[ing] that *Interstate Circuit* [*v. United States*, 306 U.S. 208 (1939)] was decided at a more advanced stage of the legal process, and we do not suggest that the same standards ought to be applied on a motion to dismiss, even under *Twombly*. However, plaintiffs argue that they have alleged enough factual matter 'to raise a reasonable expectation that discovery will reveal' circumstantial 'evidence of illegal agreement,' *Twombly*, 550 U.S. at 556, 127 S.Ct. 1955, analogous to the circumstantial evidence discovered in *Interstate Circuit*. Thus, we examine plaintiffs' complaint with an eye to any factual allegations that would make it 'reasonable' to 'expect [ ]' that similar circumstantial evidence would surface during discovery. *Id.*

583 F.3d at 906 n. 6. There is no conflict with the standard used by the Second Circuit in the Decision. Pet.App.12a, 15a n. 3.

reviewed a fully developed record (also available to the *Tam Travel* plaintiffs) and found "overwhelmingly compelling evidence that the commission cuts and caps . . . were just as likely the result of competitive conduct and natural changes in the market as of the illegal conspiracy alleged by plaintiffs." 583 F.3d at 908 n. 8, quoting *Hall*, 296 F.Supp.2d at 671, *aff'd sub nom. Hall v. American Airlines, Inc.*, 118 Fed. Appx. 680 (4th Cir. 2004). The Sixth Circuit noted that

> Although a district court decision affirmed by the Fourth Circuit is not authoritative in the Sixth Circuit, we think that the result in *Hall* is something we should at least consider (when analyzing plausibility), 'both for its persuasive power, and because it involves the same facts.' *Premier Elec. Constr. Co. v. Nat'l Elec. Contractors Ass'n, Inc.*, 814 F.2d 358, 367 (7th Cir.1987) (citation omitted) (considering Fourth Circuit decision in antitrust action involving defendants whose activities spanned more than one court of appeals). We also acknowledge the Seventh Circuit's statement in *Premier*, which warned, '[o]nly the gravest reasons should lead [a] court in [an] opt-out suit to come to a conclusion that departs from that in the class suit.' *Id.* at 367-68.

583 F.3d at 909 n. 8. Nothing in *Twombly* or *Iqbal* required the Sixth Circuit to ignore the "overwhelmingly compelling evidence" from the earlier class action. Such evidence obviously "illuminated the plausibility" of plaintiffs' claims, based on the same facts, on the motion to dismiss in the *Tam Travel* opt-out case. *Tam Travel*'s unusual procedural posture, which constrained the Sixth Circuit from reaching a

different result from that in the earlier class case except for the "gravest reasons," makes *Tam Travel* an especially poor vehicle for arguing for a "probability" standard under Rule 8.

Nor have the lower courts been "confused" by the decisions of the Second and Sixth Circuits. A district court in the Second Circuit recently dismissed an antitrust case as lacking the "robust parallel conduct allegations coupled with robust indicia of a preceding price-fixing agreement" pleaded in this case, comparing the allegations in the case before it to those in *Tam Travel*. *Anderson News, L.L.C. v. American Media, Inc.*, No. 09 Civ. 2227, 2010 WL 3001746 at *7-9 (S.D.N.Y. Aug. 2, 2010); *see also id.* at *4 ("At the pleading stage--as opposed to summary judgment stage--an antitrust complaint does not have to tend to rule out the possibility that the defendants were acting independently.") (citing *Twombly*, 550 U.S. at 556). A district court in the Sixth Circuit recently distinguished *Tam Travel* in part as an opt-out suit constrained to follow the outcome in the class action except for the "gravest reasons," and stated that in any event "*Twombly* did not purport to place on a plaintiff alleging an antitrust conspiracy claim a summary judgment standard at the pleading stage." *In re Packaged Ice Antitrust Litig.*, No. 08-MD-01952, 2010 WL 2671306 at *9 (E.D.Mich. July 1, 2010).

***Insurance Brokerage Antitrust***

Defendants assert not that *In re Insurance Brokerage Antitrust Litig.*, 618 F.3d 300 (3d Cir. 2010) is in conflict with the Decision, but that the case "attempts to chart a middle course" between the Second and Sixth Circuits. Neither contention has

merit. *Insurance Brokerage* involved allegations primarily of vertical "hub and spoke" conspiracies to allocate markets among favored insurance carriers. *Id.* at 318-19. From the 83-page opinion Defendants extract a single phrase, stating that a plaintiff relying on parallel conduct must allege at least one "plus factor," as adopting the summary judgment standard on a motion to dismiss. Petition at 25, quoting *Insurance Brokerage*, 618 F.3d at 323, quoting in turn the appeal of summary judgment in *In re Flat Glass Antitrust Litig.*, 385 F.3d 350, 360 (3d Cir.2004).

In light of *Insurance Brokerage*'s extended discussion of *Twombly*, the "plus factor" reference does not support an assertion of conflict or even a "middle course." *E.g.*:

- 618 F.3d at n. 21 ("the standards applicable to Rule 12(b)(6) and Rule 56 motions remain distinct," which Defendants ineffectively dismiss as a "cryptic observation," Petition at 25 n. 6);

- *id.* (*Twombly*'s plausibility formulation calling for "enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement," 550 U.S. at 556, "appears to support" Judge Newman's concurring opinion in this case that even allegations insufficient to go to the jury may still allow some discovery to go forward);

- *id.* at 324 n. 24 ("Sometimes, of course, discovery will uncover both direct and circumstantial evidence of agreement. We do not imply that a plaintiff must commit to a

single method of proof at the pleading stage, but merely that a plaintiff must put forth **some** statement of facts suggestive of unlawful conspiracy.") (emphasis in original);

- *id.* at 337 n. 35, citing 550 U.S. at 556 ("We note that, under *Twombly,* the test is not whether plaintiffs' allegations **necessarily** amount to an unlawful horizontal agreement, but rather whether they plausibly imply-that is, 'raise a reasonable expectation that discovery will reveal evidence of'-such an agreement.") (emphasis in original); and

- *id.* at 341 n. 42 ("As the Supreme Court reiterated in *Iqbal*, the *Twombly* standard does not impose a 'probability requirement.'") (citations omitted).

Rather than introduce "confusion and uncertainty," Petition at 27, *Insurance Brokerage* followed the *Twombly* standards and, by its own acknowledgement, found support in those standards for even the Second Circuit's concurrence in this case.

***Braden***

In *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585 (8th Cir. 2009), the Eighth Circuit reversed the dismissal of an action charging ERISA fiduciaries with breach of duty in selecting Plan investments, finding errors by the district court in ignoring reasonable inferences and in drawing inferences adverse to the non-movant. *Id.* at 595. In language only partially excerpted in the Petition (at 26), the court stated that

> there may well be lawful reasons appellees chose the challenged investment options. It is not Braden's responsibility to rebut these possibilities in his complaint, however. The district court erred by placing that burden on him, finding the complaint inadequate for failing to rule out potential lawful explanations for appellees' conduct. It stated that appellees 'could have chosen funds with higher fees for any number of reasons, including potential for higher return, lower financial risk, more services offered, or greater management flexibility.' That may be so, but Rule 8 does not require a plaintiff to plead facts tending to rebut all possible lawful explanations for a defendant's conduct.

*Id.* at 596. However, as in *Iqbal*, where there existed what in judicial experience and common sense were "more likely explanations" for defendants' conduct, a plaintiff may need to rule out [such] alternative explanations." 588 F.3d at 595-97.

> Such a requirement is neither a special rule nor a new one. It is simply a corollary of the basic plausibility requirement. An inference pressed by the plaintiff is not plausible if the facts he points to are precisely the result one would expect from lawful conduct in which the defendant is known to have engaged.

*Id.* at 597. None of this presents a conflict in light of the Second Circuit's application of the correct standards to the complaint's allegations, especially considering Defendants' inability to offer an "obvious

alternative explanation" for their conduct. *Braden* provides no reason for this Court to grant review here.

## V. DEFENDANTS FAIL TO DEMONSTRATE IMPORTANT AND RECURRING ISSUES RAISED BY THE SECOND CIRCUIT'S FACT-INTENSIVE DECISION WHICH REQUIRE RESOLUTION BY THIS COURT

Defendants reflexively warn that the Decision "will subject defendants to costly, protracted Sherman Act litigation based on nothing more than lawful conduct that is common in dynamic markets." Petition at 29. Rather than being a harbinger of "unwarranted discovery" precipitated by "deficient" and "bare-bones complaints," *id.* at 28-31, however, the Decision has been positively received as a rigorous application of this Court's Rule 8 jurisprudence applied to a fact-intensive complaint. *E.g.*, Michael B. Miller, *Clearing the Twombly Pleading Hurdle: 'Starr' Complaint Succeeds But Decision Shows Just How Strict the Standard Is*, N.Y.L.J. at S8, col. 1 (Vol. 243, June 14, 2010) (while finding that the complaint herein satisfied *Twombly*, "the Second Circuit seemed to emphasize how demanding that standard has become, rather than suggest that it is likely to be relaxed as the *Twombly* progeny grows").

> In fact, however, when one considers the scope and breadth of the factual allegations included in the *Starr* complaint, and the pains the Second Circuit took to both carefully list out the categories of relevant allegations one by one and as part of a cohesive narrative, practitioners might well conclude that *Starr* is a demonstration of just how strict the *Twombly*

> standard is proving to be in practice, not how 'lax' it might become.

*Id.* The author, who represents antitrust defendants, concludes that the court of appeals' decision should not be read as an attempt to "soften *Twombly*'s impact."

Indeed, empirical evidence shows not that *Twombly* is being loosely enforced, but that motions to dismiss are being granted with greater frequency since *Twombly* and *Iqbal* were decided.

> A recent study of randomly selected federal civil cases (all cases, not just antitrust) found that, pre-*Twombly*, Rule 12(b) (6) motions were granted 46 percent of the time; post-*Iqbal* that number had increased to 56 percent. The study's author took the analysis a step further, conducting a 'multinomial logistic regression' that indicated a Rule 12(b)(6) motion under *Twombly* was 1.81 times more likely to be granted with leave to amend rather than denied than under *Conley* [*v. Gibson*, 355 U.S. 41 (1957)], and under *Iqbal* those odds increased to more than four times greater than under *Conley*.

*Id.* (citing Patricia Hatmayer, *The Tao of Pleading: Do Twombly and Iqbal Matter Empirically?* 59 AM. U. L. REV. 553, 556 (2010)).

Defendants fail to demonstrate any recurring issues arising from the fact-bound Decision requiring resolution by this Court.

## CONCLUSION

The petition for writ of certiorari should be denied.

Dated: November 22, 2010

Respectfully submitted,
CHRISTOPHER LOVELL
*Counsel of Record*
GARY S. JACOBSON
LOVELL STEWART HALEBIAN
JACOBSON LLP
61 Broadway, Suite 501
New York, NY 10006
(212) 608-1900
clovell@lshllp.com

JOHN J. STOIA, JR.
BONNY E. SWEENEY
ROBBINS GELLER RUDMAN
& DOWD LLP
655 West Broadway, Suite 1900
San Diego, CA 92101
(619) 231-1058

*Counsel for Respondents*

No. 10-263

IN THE

# Supreme Court of the United States

SONY MUSIC ENTERTAINMENT, ET AL.,

*Petitioners*,

v.

KEVIN STARR, ET AL.,

*Respondents*.

**On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit**

## REPLY BRIEF FOR PETITIONERS

THOMAS G. HUNGAR
*Counsel of Record*
JOSEPH KATTAN, PC
THOMAS M. JOHNSON, JR.
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 955-8500
thungar@gibsondunn.com

*Counsel for Petitioners*

## RULE 29.6 STATEMENT

The corporate disclosure statement included in the petition for a writ of certiorari remains accurate.

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## REPLY BRIEF FOR PETITIONERS

Despite plaintiffs' attempts to confuse the nature of the issues and distract the Court's attention from the question presented, there is no dispute that the Second Circuit squarely held that the substantive legal standard applicable to plaintiffs' claim at summary judgment and trial does not govern at the pleading stage. Pet. 3, 9; Opp. 27. That holding is in conflict with this Court's precedents and inconsistent with decisions of other courts of appeals, and merits this Court's review.

Plaintiffs' principal response is that petitioners seek to impose a "probability" standard on allegations in a complaint, but that argument is baseless. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), establishes the governing procedural requisites at the motion-to-dismiss stage—plaintiffs must allege facts establishing a "plausible entitlement to relief" (*id.* at 559)—but the substantive standard governing the claim remains the same at each stage of the case. Here, that standard requires plaintiffs to allege facts that plausibly "tend to exclude" independent, self-interested conduct as an explanation for the defendants' alleged behavior.

Plaintiffs' remaining attempts to obscure the clarity of the question presented are without merit and provide no basis for denying review.

### I. THE SECOND CIRCUIT'S DECISION CONFLICTS WITH *TWOMBLY* AND *IQBAL*

Under *Twombly* and *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009), plaintiffs must plead facts that plausibly show "entitlement to relief" (*Twombly*, 550 U.S. at 559); that is, facts that could satisfy the substantive legal standards that would govern the claim at summary judgment or trial. Pet. 12-16; *see also*

*Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 346 (2005). Plaintiffs argue that this rule would create a "probability" standard at the pleading stage. Opp. 11. It does not.

Plaintiffs are not required to prove their case at the pleading stage or show that it is more likely than not they will prevail; but they must allege facts that show a "plausible entitlement to relief." *Twombly*, 550 U.S. at 559. To be sure, the *procedural* requisites change at later stages of litigation: At summary judgment, a plaintiff may proceed to trial only if the evidence obtained during discovery raises a "genuine dispute as to [a] material fact" (Fed. R. Civ. P. 56(a)), and a plaintiff must have "a legally sufficient evidentiary basis" for a favorable ruling to avoid a directed verdict (*id.* 50(a)(1)). But while the procedural standards differ at each stage of a case, the substantive legal standard remains constant.

Despite plaintiffs' claim that "[n]o court has adopted [the] argument that *Twombly* and *Iqbal* . . . require . . . that [a] complaint allege facts sufficient to 'satisfy the same substantive legal standard that applies at summary judgment or trial'" (Opp. 11), that was precisely this Court's mode of analysis in *Twombly* and *Iqbal* themselves. In *Twombly*, the Court analyzed antitrust cases decided at the summary judgment, directed verdict, and trial stages. *See* Pet. 12-14. The Court concluded that because, *at those later stages*, evidence of parallel conduct alone is insufficient to state a claim for unlawful conspiracy, the same standard applied to the allegations in the complaint at the pleading stage. *See id.*

In *Iqbal*, the Court likewise examined cases decided at summary judgment and trial, and concluded that because plaintiffs must *prove* unlawful intent at those stages, they must also *plead* unlawful intent in

their complaint. *See* Pet. at 14-15; *accord Dura*, 544 U.S. at 346.

Plaintiffs' reading of *Twombly* finds no refuge in this Court's discussion of Judge Lynch's district court opinion in that case. 550 U.S. at 552. Refuting plaintiffs' attempt (Opp. at 17-18) to suggest that his opinion limited the "tends to exclude" standard to the summary judgment phase, Judge Lynch explicitly stated that "district courts have required" plaintiffs to meet that same standard "in order to withstand motions to dismiss." *Twombly v. Bell Atl. Corp.*, 313 F. Supp. 2d 174, 179-80 (S.D.N.Y. 2003). The court below read Judge Lynch's opinion the same way: "the district court [in *Twombly*] . . . held that plaintiffs must allege additional facts that tended to exclude independent, self-interested conduct." Pet. App. 18. This Court approvingly cited that reasoning in *Twombly*, 550 U.S. at 552, and it directly conflicts with the Second Circuit's decision here.

Plaintiffs also attempt to find support for their position in *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506 (2002). But *Twombly* clarified that *Swierkiewicz* held only that a plaintiff need not engage in "heightened fact pleading of specifics" if the facts contained in a complaint suffice to state a claim for relief. 550 U.S. at 570. It was plausible that the allegations in *Swierkiewicz* would be substantiated by direct evidence of discrimination, and thus this Court did not require the plaintiff to "allege certain additional facts that [he] would need at the trial stage to support his claim *in the absence of direct evidence*." *Id.* (emphasis added); *see* Pet. 16 n.3. But this Court did not hold that a complaint could survive a motion to dismiss without pleading facts consistent with *any* substantive theory of liability. That is what the plaintiffs attempted to do in *Twombly*, and what plaintiffs attempt to do here.

In short, plaintiffs are unable to explain away the conflict between the decision below and *Twombly*, *Iqbal*, and *Dura*. Moreover, even if there were some remaining confusion regarding the import of *Swierkiewicz* in light of *Twombly* and *Iqbal*—and there is not—that would hardly militate against further review. Instead, it would simply confirm the need for this Court to grant certiorari and clarify the important issue of law presented by the petition.

## II. THE HOLDING BELOW CONFLICTS WITH DECISIONS OF OTHER COURTS OF APPEALS

Plaintiffs' analysis of decisions from other circuits does nothing to diminish the conflict among the courts of appeals on the proper substantive standard to apply when evaluating the plausibility of allegations in a complaint.

*First*, plaintiffs do not dispute that the Third Circuit recently held that "plaintiffs relying on parallel conduct must allege facts that, if true, would establish at least one 'plus factor,' since plus factors are, by definition, facts that 'tend[] to ensure that courts punish concerted action—an actual agreement—instead of the unilateral, independent conduct of competitors.'" *In re Ins. Brokerage Antitrust Litig.*, 618 F.3d 300, 323 (3d Cir. 2010) (citation omitted); *see also* Opp. 32. Plaintiffs downplay this holding as a "single phrase" in a long opinion (Opp. 32-33), but it is nonetheless an explicit holding of the Third Circuit, binding on all federal courts in that circuit. And that holding conflicts with the decision below, which held that plaintiffs can survive a motion to dismiss without pleading *any* factors tending to exclude the possibility of independent action.

*Second*, plaintiffs do not dispute that the Eighth Circuit has held that, where "obvious alternative ex-

planation[s]" exist for a defendant's conduct, "a plaintiff may be required to plead additional facts tending to rule out the alternative." *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585, 597 (8th Cir. 2009); *see also* Opp. 34. They simply object that petitioners failed to offer an "obvious alternative explanation" here, which—as explained below—is incorrect. *See infra* pp. 8-9.

*Third*, plaintiffs do not dispute that the Sixth Circuit held that the "tends to exclude" standard "illuminates the plausibility" of allegations in antitrust complaints. *Tam Travel, Inc. v. Delta Airlines, Inc.*, 583 F.3d 896, 907 n.7 (6th Cir. 2009); *see also* Opp. 28. They merely point out that the court did not explicitly state that plaintiffs are required to plead such facts. But unlike the Second Circuit, the Sixth Circuit clearly held that the summary-judgment standard was *relevant* in determining whether a complaint's allegations were plausible. That mode of analysis cannot be reconciled with the decision below. [1]

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[1] The decision below is also inconsistent with the Eleventh Circuit's recent decision in *Jacobs v. Tempur-Pedic Int'l, Inc.*, No. 08-12720, 2010 WL 4880864 (11th Cir. Dec. 2, 2010). Relying on *Twombly* and *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986) (2010 WL 4880864, at *9-*10), the court dismissed an antitrust conspiracy claim because the plaintiffs did not meet their "burden to present allegations showing why it is more plausible" that the alleged co-conspirators "would enter in an illegal price-fixing agreement . . . to reach the same result realized by purely rational profit-maximizing behavior." *Id.* at *9. *Jacobs* cannot be squared with the Second Circuit's holding that plaintiffs can survive a motion to dismiss without pleading any factors that plausibly tend to exclude the possibility of independent action.

## III. THERE ARE NO CASE-SPECIFIC OBSTACLES TO THIS COURT'S RESOLUTION OF THE QUESTION PRESENTED

Plaintiffs attempt to avoid review by characterizing the decision below as fact-dependent and accusing petitioners of failing to refute specific facts in the complaint. These arguments are without merit.

**1.** Plaintiffs complain that petitioners failed to explain how two statements by industry executives alleged in the complaint could be consistent with independent, self-interested conduct. Opp. 10-11. Plaintiffs mischaracterize these statements and fail to explain how this argument counsels against certiorari.

The Second Circuit committed a pure error of law: It held that plaintiffs were not required to plead facts sufficient to raise a plausible claim of entitlement to relief under the substantive legal standard governing their claim, which requires that the proffered facts "tend to exclude" independent, self-interested behavior. Pet. App. 18. That the court of appeals considered "fourteen separate facts" in conducting its analysis is *irrelevant* (Opp. 2)—it did so under the wrong substantive standard.

In any event, petitioners demonstrated below that plaintiffs' allegations do not plausibly show entitlement to relief, because they describe the lawful behavior of joint ventures setting the prices and terms of the venture's own products. *See* Mem. in Support of Defs.' Mot. to Dismiss 11 & n.8 ("[I]t is well-established that joint ventures are free to set the terms and requirements under which the joint venture will operate."); Appellees' Br. 27 (same). That is a complete response to the two statements cited by plaintiffs.

First, plaintiffs mischaracterize (through use of a bracketed insertion) a quotation by Edgar Bronfman, Jr., currently CEO of Warner Music Group (one of the petitioners). According to plaintiffs, he stated that "we [the *music industry*] determine" Internet Music prices. Opp. i (emphasis added). To the contrary, Bronfman's quotation referred to *pressplay*, one of the two joint ventures, setting the price for its own product sold by its agent distributors. Pet. App. 93a ("*Pressplay* has what we call an affiliate model where *we determine the price*, and we offer a percentage of that price to the retailing partner . . .") (emphasis added). It is lawful for members of a joint venture to set the prices that the *joint venture* will charge for its products (*see Texaco Inc. v. Dagher*, 547 U.S. 1, 8 (2006)), and it is indisputably within each member's self-interest to do so.

Second, plaintiffs point to an industry executive's statement that there are "legal/antitrust reasons" why a "most favored nation[]" clause should be included in an alleged side letter rather than in a licensing agreement between EMI and its joint venture, MusicNet. Opp. 3; Pet. App. 95a.[2] According to the complaint, this letter memorialized an agreement that EMI's economic terms would be as favorable as those of the other two co-venturers in MusicNet. Pet. App. 95a (¶¶ 94, 95). There is nothing anticompetitive or contrary to individual self-interest about an agreement among co-venturers to enter their common enterprise on an equal footing. *See Dagher*, 547 U.S. at 8. And in any event, a nonlawyer's speculations about the appearance of im-

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[2] Plaintiffs attribute this comment to Rob Glaser, erroneously identified as "EMI CEO." Pet. App. 95a (¶ 95). It is a matter of public record that Mr. Glaser worked for MusicNet, not EMI.

propriety under antitrust law does not plausibly allege a conspiracy.

**2.** Plaintiffs concede that the Second Circuit was obligated to consider "'obvious alternative explanation[s]'" for petitioners' conduct, and "'to draw on its judicial experience and common sense'" in reviewing the complaint. Opp. 24 (quoting *Iqbal*, 129 S. Ct. at 1950). They argue, however, that there was no "obvious alternative explanation" here, because petitioners "have not explained how their alleged conduct made economic or common sense as a response to 'Internet piracy.'" Opp. 25.

Plaintiffs are wrong. An industry commentator stated in an article on which plaintiffs' complaint relies that petitioners' motivation in forming the joint ventures was to "'protect their copyrighted works from freewheeling swapping on the Internet, and to pick up a few extra bucks for making the music available digitally.'" Pet. 22 n.5 (quoting Tom Spring, *Digital Music: Worth Buying Yet?*, PC World, Jan. 18, 2002); Pet. App. 89a n.2. Plaintiffs cannot credibly claim that the article on which they heavily rely fails to "comport with common sense." Opp. 24.

Moreover, contrary to plaintiffs' claims, petitioners explained in the lower courts that "[t]he joint ventures, in order to control piracy, restricted their subscribers to 'tethered' downloads or 'streams' so that a subscriber could not capture a song file on his or her computer and transfer it to non-subscribers, portable devices or CDs." Appellees' Br. 12 n.7; *see also* Mem. in Support of Defs.' Mot. to Dismiss 16-17 (similar). As the district court understood, usage restrictions made perfect sense as a "collaborative effort to address widespread music piracy." Pet. App. 45a.

Contrary to plaintiffs' conspiracy allegations, it is much more plausible that the joint ventures were

unprofitable because petitioners were unsuccessful in their initial attempt to package and sell Internet Music in a form that was attractive to consumers while also protecting their copyrighted work from Internet piracy. The court of appeals' failure to consider this "obvious alternative explanation" conflicts with *Twombly* and *Iqbal*.

Because the erroneous legal principle adopted by the court of appeals conflicts with *Twombly*, *Iqbal*, and *Dura* and will create confusion for courts attempting to apply this Court's precedents, certiorari is warranted to resolve that conflict. *See* Pet. 12-16. If this Court were to grant review and correct (for a third time) the Second Circuit's erroneous approach to assessing pleadings at the motion-to-dismiss stage, the Court in its discretion could (as in *Twombly* and *Iqbal*) then proceed to apply that standard to the allegations of the complaint, but such an approach would serve only to provide further guidance for the lower courts.[3]

## IV. THE QUESTION PRESENTED WAS BOTH PRESSED AND PASSED UPON

Their other arguments unavailing, plaintiffs fall back on the baseless claim that the question presented was waived below. Opp. 26-27. But waiver occurs "only when the question presented was not pressed or passed upon below" — a "rule [that] operates (as it is phrased) in the disjunctive." *United States v. Williams*, 504 U.S. 36, 41 (1992). The issue

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[3] Alternatively, of course, the Court could remand for further proceedings. That course would not be necessary here: The district court, under the correct legal standard, had no difficulty ruling for petitioners. Pet. App. 32a-67a. Indeed, plaintiffs do not even contend that their complaint could pass muster under that standard.

here was *both* pressed *and* passed upon, and is therefore squarely presented.

Petitioners devoted an entire section of their appellate brief to the argument that "The 'Tends To Exclude' Standard Applies At The Motion To Dismiss Phase." Appellees' Br. 15-19. And as plaintiffs admit (Opp. 27), the Second Circuit explicitly considered, and rejected as "incorrect," petitioners' argument to that effect. Pet. App. 18a. The Second Circuit thus held that a plaintiff alleging a Section 1 violation need not test a complaint's plausibility against the substantive legal standard that governs at summary judgment or trial. That is precisely the issue on which petitioners seek this Court's review.[4]

## V. POLICY CONSIDERATIONS SUPPORT THIS COURT'S REVIEW

Finally, the policy concerns advanced by plaintiffs do not counsel against certiorari.

Plaintiffs claim that the legal standard advanced by petitioners would promote "corporate self-interest and the market" over "judicial and regulatory deterrence." Opp. 1. *Dura*, *Twombly*, and *Iqbal*, however, establish an equal-opportunity pleading standard that applies to *all* federal causes of action, regardless of the identity of the parties. *See Iqbal*, 129 S. Ct. at 1952.

Plaintiffs also argue that the Court should accept the view expressed in an antitrust treatise that the

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[4] Plaintiffs also fault petitioners for citing *Dura*, 544 U.S. 336, for the first time in their petition for certiorari. Opp. 22. When, as here, the question presented was pressed and passed upon below, however, this Court will not deem the issue waived merely for failure to cite a specific authority in the court of appeals. *See generally* Eugene Gressman et al., *Supreme Court Practice* 6.26(b) (9th ed. 2007).

"tends to exclude" standard does not apply at the pleading stage. Opp. 13 & n.7. This Court need hardly defer to a particular academic opinion on an issue of pleading standards. In any event, other commentators have read *Twombly* to require the pleading of facts that satisfy the legal standard applicable at summary judgment or trial.[5] That the question presented has drawn scholarly commentary and debate simply illustrates its importance and confirms the need for this Court's review to resolve the conflict by clarifying the appropriate legal rule.

## CONCLUSION

For the reasons stated herein and in the petition, certiorari should be granted. The Court may wish to consider summary reversal.

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[5] *See, e.g.*, Mark Anderson & Max Huffman, Iqbal, Twombly, *and the Expected Cost of False Positive Error*, 20 Cornell J.L. & Pub. Pol'y 1, 52 (2010) (describing the "essential step required of circumstantial allegations by *Twombly* of tending to exclude the possibility of unilateral conduct"); A. Benjamin Spencer, *Plausibility Pleading*, 49 B.C. L. Rev. 431, 450 (2008) ("[I]t seems . . . the Court . . . held that the additional evidence that will be required at trial (and at the summary judgment stage) to prove an agreement based on parallel conduct—evidence that must tend to exclude the possibility of independent action—must be alleged at the pleading stage.") (footnote omitted).

Respectfully submitted.

THOMAS G. HUNGAR
*Counsel of Record*
JOSEPH KATTAN, PC
THOMAS M. JOHNSON, JR.
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 955-8500

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